

dence to show that such coverage ratios must be maintained at levels comparable to those of 1954 and prior years, nor is there evidence of comparability with other companies and industries to show that the quality of Tennessee's senior securities will suffer in the market place if Tennessee is not given the 7 percent rate of return which it seeks.

There is likewise no substantial evidence to support Tennessee's contention that it needs a 14 to 15 percent return on common equity because certain electric utilities have had an average return of almost 11 percent over a period of years. We are not convinced that the selection of electric utilities made by Tennessee presents a proper basis for comparison, or that the differing risks inherent in the two industries can be measured as Tennessee here proposes. It is significant to note that according to Tennessee's own study, the three largest electric utilities for which data is shown—namely, Consolidated Edison Company of New York, Pacific Gas and Electric Company and Public Service Electric and Gas Company—had earnings on common equity for 1958 of 8.1, 9.7 and 8.6 percent, respectively.

Upon consideration of the earnings-price ratio data and all the factors discussed above, and giving consideration to the corporate costs of equity financing, we conclude that an allowance on common equity of between 10 and 10.5 percent is fully adequate for Tennessee, and is sufficient to enable Tennessee to attract new equity capital and preserve its financial integrity. As indicated in the table set forth above, an overall rate of return of $6\frac{1}{8}$ percent will provide Tennessee an allowance of 10.12 percent on its common equity, and we shall therefore fix the fair, just and reasonable rate of return to Tennessee for the purpose of this interim order at $6\frac{1}{8}$ percent.

The overall rate of return so determined is applicable to all of Tennessee's properties, including well-mouth pro-

duction properties. Tennessee has not urged, nor does the record at this point in the proceeding show, that Tennessee is entitled to any different rate or return on its production properties. This question, however, is bound up with the question of the treatment of tax benefits for statutory depletion and intangible well drilling costs, which we are reserving for disposition in the next phase of the proceeding. Thus final determination of the proper rate of return on production properties cannot be made at this time, but will be made upon conclusion of the next phase of the proceeding.

IMMEDIATE REFUNDS

The propriety and legality of ordering immediate refunds of amounts which Tennessee has collected subject to refund since April 5, 1960, has been settled by our recent order in the *Southern Natural* case, *supra*. The purpose of the interim order procedure is to alleviate, to the extent possible, the financial burden of increased rates being borne by Tennessee's

5379

wholesale gas customers. The record shows that if the rate of return herein determined were 6 percent, the effect of such rate of return and associated income taxes would result in savings to these customers during the interim period in the amount of \$13,037,649 a year. Although the savings will be somewhat less on the basis of the 6 $\frac{1}{4}$ percent rate of return herein determined, the amount of the savings are of such magnitude that the public interest requires disallowance of Tennessee's proposed rates and a fling of substitute rates based on the 6 $\frac{1}{4}$ percent rate of return, such substitute lower rates to be effective as of April 5, 1960.

Immediate refunds of the increased rates collected by Tennessee since April 5, 1960, to the extent that such rates

exceed the substitute lower rates based on the $6\frac{1}{8}$ percent rate of return, will put Tennessee and its customers in the same position that they would be in had Tennessee initially filed its increased rates on the basis of the $6\frac{1}{8}$ percent rate of return which we here find to be the proper rate of return. Tennessee should not be permitted to retain amounts which it has collected on the basis of an unlawful rate of return, and we shall therefore order immediate refunds of these amounts.

Tennessee argues here, as did Southern in the *Southern Natural* case, that the interim order procedure is unlawful and inequitable unless the Commission makes final disposition of the complex issues of cost allocation and rate design at the same time it determines the proper rate of return, since Tennessee may not be able to recover its cost of service should the Commission decide these issues in such a way that Tennessee would have to make refunds in certain zones where its rates are found to be too high but could recover revenues retroactively in those zones where it has charged less than the finally determined cost of service. This argument was fully answered by us in the *Southern Natural* order where we concluded (mimeo. page 3):

"Should Southern suffer legal injury by reason of the Commission's final order in the second phase of this proceeding, it may seek judicial review. It cannot, however, be heard to complain of an order which fixes a proper rate of return and looks only to the establishment of interim rate levels based on such proper return and which in all other respects are based on the methods and procedures employed by Southern in making its rate filing, including its own allocation and rate design methods.

Certain of the intervening customer companies have expressed the fear that their right to receive funds of all

amounts collected from them by Tennessee, in excess of what is finally determined upon the conclusion of the next phase of the proceeding to be just and reasonable, will be prejudiced by an order at this time directing interim refunds upon the allocation and rate design methods proposed by Tennessee. We cannot agree that these customers will be so prejudiced by this interim order. As noted above, this order serves to place such customers in the same position

5380

as if Tennessee had initially filed its proposed increased rates utilizing the rate of return which we herein find to be proper. Tennessee's customers will be afforded all the protection provided by the terms of the Natural Gas Act.

The Commission finds:

(1) The fair, just and reasonable rate of return to be allowed Tennessee in this proceeding is $6\frac{1}{8}$ percent; subject, however, to final disposition in the next phase of this proceeding of the related issues as to accumulated deferred taxes and tax benefits for statutory depletion and intangible drilling expenses, and final determination of the rate of return to be allowed Tennessee with respect to its well-mouth production properties; and subject to such further consideration as may be required in light of additional evidence which shall be presented in the next phase of the proceeding to show Tennessee's capitalization insofar as it applies only to Tennessee's gas pipeline business.

(2) The proposed increased rates filed in this proceeding by Tennessee, and presently being collected by Tennessee subject to refund under the order of the Commission issued April 29, 1960, whereby the proposed increased rates became effective as of April 5, 1960, are excessive and should be disallowed.

(5380)

(3) Tennessee should be permitted to file herein substitute lower rates satisfactory to the Commission, based on the $6\frac{1}{8}$ percent rate of return herein found to be proper for the purpose of this interim order, such substitute lower rates to become effective as of April 5, 1960, upon acceptance by the Commission, subject to refund in accordance with the Commission's order of April 29, 1960, and the undertaking heretofore filed by Tennessee in accordance with the terms of that order.

(4) Tennessee should be required to make prompt refunds with interest at 7 percent, in accordance with the Commission's order of April 29, 1960, and the undertaking heretofore filed by Tennessee, of all amounts collected by it from its jurisdictional customers subject to refund under its proposed increased rates; provided, however, that if Tennessee files substitute lower rates as herein provided, the amount of such refunds should be the excess of the amounts so collected over what it would have collected on the basis of the substitute lower rates so filed and found to be satisfactory by the Commission. A plan for making such refunds should be submitted for approval of the Commission.

The Commission orders:

(A) The proposed increased rates filed in this proceeding by Tennessee are hereby disallowed.

5381

(B) Tennessee may, within 15 days of the date of this order, file in lieu thereof appropriate substitute tariff sheets to its FPC Gas Tariffs containing lower rates satisfactory to the Commission, based on the $6\frac{1}{8}$ percent rate of return herein found to be proper for the purpose of this interim order. Tennessee shall accompany its substitute filing with supporting cost of service and allocation data, to be

computed and presented in the same form and manner as contained in its exhibits heretofore offered by it in this proceeding, revised only to reflect a 61s percent rate of return and Federal income taxes associated therewith. Tennessee shall further furnish with its filing a statement setting forth the method of computation of such substitute rates and showing the derivation thereof. Tennessee shall also accompany its substitute tariff sheets and supporting data with a certificate showing service of copies thereof on all purchasers under the rate schedules involved, interveners in this proceeding, and interested state commissions. Comments by such parties shall be submitted to the Commission within ten days after service by Tennessee as required herein.

(C) Upon acceptance of such filing of substitute rates as satisfactory to the Commission, the rates, charges and classifications set forth in Tennessee's substitute tariff sheets shall become effective as of April 5, 1960, subject to refund, in accordance with the Commission's order of April 29, 1960, and the undertaking heretofore filed by Tennessee in compliance with the terms of that order, and subject to further orders of the Commission in this proceeding.

(D) Tennessee shall, within 15 days of the date of this order, file with the Commission its plan for promptly refunding to its jurisdictional customers the amounts which by finding paragraph (4) the Commission has found should be refunded by this order. Tennessee shall accompany its plan for refunds with a statement setting forth the computation of the refunds and interest, and the derivation thereof. Tennessee shall also accompany its plan for refunds and supporting statement with a certificate showing service of copies thereof on all purchasers under the rate schedules involved, interveners in this proceeding, and interested state commissions. Comments by such parties shall be submitted to the Commission within ten days after

(5381)

service by Tennessee as required herein. Upon approval by the Commission of said plan of refunding Tennessee shall make the refunds as so approved within 30 days thereafter, and shall report to the Commission within said 30 days the amounts so refunded to each jurisdictional customer.

(F) Tennessee shall, in the next phase of this proceeding, present additional evidence to show its capitalization insofar as it applies only to its gas pipeline business, as more fully discussed in the body of this order.

5382

(F) The issues as to accumulated deferred taxes and tax benefits for statutory depletion and intangible well drilling expenses, and final determination of the rate of return on Tennessee's well-mouth production properties, shall be reserved for the next phase of this proceeding, together with all other issues as yet undisposed of, and further consideration shall be given at that time to the additional evidence with respect to rate of return presented by Tennessee in accordance with paragraph (E) above.

(G). This order is without prejudice to further hearings in this proceeding on the reserved issues not herein decided and to such further order or orders as the Commission may issue in the disposition of the reserved issues and in final disposition of this proceeding.

By the Commission. Chairman Kuykendall dissents and states he would allow a rate of return of $6\frac{1}{4}\%$.

J. H. GUTRIDE
Joseph H. Gutride
Secretary.

5420

UNITED STATES OF AMERICA
BEFORE THE FEDERAL POWER COMMISSION

Docket No. G-19983

In the Matter of

TENNESSEE GAS TRANSMISSION COMPANY

**Application of Tennessee Gas Transmission Company
For Rehearing of Order Issued August 9, 1960**

Tennessee Gas Transmission Company (Tennessee), being aggrieved by the Commission's "Order Determining Rate of Return Disallowing Proposed Increased Rates and Directing Payment of Refunds and Permitting Substitution of Lower Interim Rates," issued herein on August 9, 1960, hereby applies, pursuant to Section 19 of the Natural Gas Act and Section 1.34 of the Commission's Rules of Practice and Procedure, for rehearing of that order. The grounds upon which this application is based are set forth below.

Preliminary Statement

This is not a perfunctory application for rehearing filed solely to perfect an appeal to the Court. It is, rather, an earnest appeal to the conscience and judgment of this Commission to prevent grave injustice and irreparable harm to Tennessee, its investors and the public which it serves. The Commission's order is so shocking, and its impact upon Tennessee's financial integrity and ability to continue to render adequate service to the public so adverse, as to overwhelmingly require the granting of this application for rehearing.

5421

Since its birth in 1944, Tennessee has faithfully rendered complete and adequate service to its customers. It has

(5421)

expanded faster than any other natural-gas company in the country in an effort to meet the growing needs of the public for natural gas. Its stockholders have invested hundreds of millions of dollars in good faith in reliance upon the enlightened past policy of the Commission of allowing a fair rate of return on the common equity of Tennessee. The Commission's order constitutes an abrupt and cruel reversal of such past established policy which is so drastic in its consequences as to lead to the inevitable conclusion that the order is arbitrary and lacks a rational basis.

The violent change in the Commission's past policy and the destructive force of the Commission's order can be readily demonstrated. In Tennessee's previous rate case (Docket G-5259) the Commission expressly found that rates fixed on the basis of a 6 percent rate of return were "*just and reasonable*." (18 F.P.C. 428, 437). That finding was based on the financial facts shown in that record for the year 1955 (18 F.P.C. at p. 441).¹ Since that time, yields on "A" bonds have increased by 54 percent; yields on U.S. Government bonds have increased 43 percent; and the average cost of Tennessee's total long-term debt has increased 24 percent. Yet, the Commission's present order increases Tennessee's over-all rate of return from 6 percent to 6 1/8 percent, an increase of

5422

only 2.1 percent. It is obvious at once that what the Commission has done here is to require Tennessee's stockholders to absorb virtually the entire 24 percent increase in the cost of long-term debt which Tennessee has incurred since 1955. The irony of this is that the increased cost of the long-term debt was the direct result of Tennessee's expansion of its system capacity to meet the growing gas require-

¹ Some 36 pages of detailed statistical data on rate of return were presented in that case through a Staff expert witness, in addition to the evidence on rate of return presented by Tennessee.

ments of the public. If Tennessee had failed to expand, it would not have incurred this increased cost of debt and it would not have been necessary to seek the higher rate of return applied for in this case. Under those circumstances, Tennessee's stockholders would have continued to enjoy the return which the Commission allowed to them in the previous rate case without seeking any increase in the rate of return. In short, the "reward" which the Commission's present order gives Tennessee's stockholders for expanding its system capacity to meet the increased gas requirements of its customers is a *reduction* in the return on their book equity from the rate of 13.71 percent previously allowed in Docket G-5259² to only 10.12 percent in this case. This is a *reduction* of 26 percent. Does this Commission really believe that the stockholders of Tennessee will be encouraged to expand capacity in the future after having thus been "rewarded" with a 26 percent cut in their earnings for having expanded Tennessee's capacity during the past four years?

It is evident that the Commission's interim order places in serious jeopardy, if it does not completely prevent, any further significant expansion of Tennessee's jurisdictional pipeline business. Indeed, so

5423

serious is the threat of the Commission's order to Tennessee's plans for future expansion that the company has found it necessary to reconsider the feasibility of going forward with the expansion program applied for in Docket CP60-94, and is requesting the Commission to hold in abeyance all action in connection with its application in that docket pending re-examination and further study of the feasibility of that project in the light of the Commission's interim order.

² 18 F.P.C. at p. 441.

Will the Commission's return of $6\frac{1}{8}$ percent encourage expansion? Certainly not. On the contrary, it discourages expansion for the simple reason that under the Commission's new and destructive policy of requiring the stockholders to absorb the higher cost of debt incurred in financing new facilities, they stand to lose more ground with each succeeding step of expansion. A simple illustration will serve to demonstrate the erosion that takes place in the equity position under the Commission's order. Assume that each \$100 of additional capital raised for financing expansion consists of \$57 of bonds, \$14 of preferred stock and \$29 of common stock, which is the approximate capitalization ratio shown on page 3 of the order. With the present day cost of bonds and preferred stock hovering around $5\frac{1}{2}$ percent, the Commission's over-all rate of return of $6\frac{1}{8}$ percent will yield a return for such new common equity increment of only 7.6 percent. How, we ask, can new equity capital be attracted to this enterprise for such a paltry reward?

Tennessee was born under F.P.C. regulation. It has expanded and financed under the watchful eye of this Commission. Its rates have been under constant surveillance by the Commission. Investors have poured

5424

many hundreds of millions of dollars into this enterprise in good faith and reliance upon the past decisions of this Commission on Tennessee's certificate and rate matters. The Commission has consistently, since Tennessee's birth in 1944, allowed Tennessee to charge rates which enabled it to earn a rate of return in the neighborhood of 14 percent on its common book equity. The hundreds of thousands of persons and institutions who invested their money in the common stock of Tennessee over the years paid prices for that stock which reflected such earnings. In so doing they

relied upon the previous rate orders of this Commission which found that Tennessee's rates fixed on this basis were "just and reasonable." Stated another way, they relied upon a continuation of the past policy of the Commission with regard to the determination of the fair and reasonable return on common book equity. The Commission cannot now brush aside the responsibility for the consequences of its action in arbitrarily cutting the return on Tennessee's equity by 26 percent with the more general observation that "There is no sound basis for Tennessee's claim that it is entitled to the same return on book equity which it has historically enjoyed."³ (p. 6 of order). It cannot be gainsaid that it was the Commission's own action in maintaining a consistent policy in numerous Tennessee rate cases over the past 16 years which formed the basis in the minds of investors for the belief that such policy would be continued in the future.

The return here allowed on Tennessee's common book equity is far and away the lowest ever allowed to Tennessee. Indeed, it is the lowest ever allowed by the Commission on an equity of such thickness to any

5425

natural-gas company in the past decade. The Commission has recently indicated that it is not oblivious of the fact that the cost of money has risen in recent times. It recently required natural-gas companies to increase the rate of interest on refunds to customers from 6 percent to 7 percent. It very recently increased the rate of return to two other natural-gas companies, namely Southern Natural Gas Company (Docket G-20509) and Manufacturers Light and Heat Company, to 6½ percent (23 F.P.C. 446).

³ As shown later herein, Tennessee is not claiming the same return on its common book equity which it previously enjoyed, but rather is claiming an equivalent return (12.5%) on its present thicker book equity.

(5425)

In so doing, the Commission allowed those companies to earn higher rates of return than Tennessee on their common book equities in the face of the fact that such equities were thicker and hence less risky than that of Tennessee. Such rank discrimination against Tennessee defies our understanding.

It has been the Commission's consistent and sound policy since the passage of the Natural Gas Act to allow a fairly uniform over-all rate of return to the natural-gas industry. The result of this sound policy was to consistently allow higher returns on thinner and less secure common equities than on thicker and more secure common equities. And, as the Commission knows, the industry has expanded and serve the public well under such policy. As we read the Commission's recent orders, that policy has now been abruptly reversed. The Commission now allows a uniform rate of return (around 10 percent) on common book equity, irrespective of the thickness or thinness of such equity. This new policy has produced the absurd and discriminatory result of allowing a higher over-all rate of return to those companies having thicker and, therefore, less risky equities than to those having thinner and, therefore, more risky equities. This reversal of policy simply does not make economic and financial sense. If pursued it will convert the natural-gas pipeline business from a strong and healthy industry into a sick industry.

5426

Additionally, as more fully shown below, the interim decision procedure adopted by the Commission is clearly unlawful. The Natural Gas Act requires the Commission to first find that the filed rates are "unjust, unreasonable, unduly discriminatory, or preferential" before it can prescribe different rates. It cannot now enter such a finding because it has not yet decided the allocation issue which

holds the key to the question of whether the filed rates are too high or too low in any of the six zones. The Act also requires the Commission to determine and fix the "just and reasonable" rate to be charged "after full hearing." The Commission has not yet held "full hearings" on all issues affecting the reasonableness of the filed rates, and it has failed and refused to decide the allocation issue, without which it cannot determine what rates shall be prescribed for the various zones. Instead of fixing rates as required by the Act, the Commission has unlawfully attempted to delegate, under pain of economic sanctions to Tennessee the responsibility of fixing the rates to be charged under the interim order and, in so doing, to assume the risk of not being able to recover its cost of service depending on the outcome of the Commission's later decision on the allocation issue. The glaring unfairness of such interim order procedure is even more apparent when it is recognized that the allocation issue has been fully tried during the past three years, has been fully briefed, and has been ripe for decision for several months. There is no excuse for the Commission to place Tennessee in jeopardy of not recovering its cost of service, including even the meagre $6\frac{1}{8}$ percent rate of return allowance, simply because the Commission arbitrarily refuses to decide an issue which is now ripe for decision.

5427

I

Rate of Return

The Commission, in the order here involved, concluded that a rate of return of $6\frac{1}{8}$ percent is "the fair, just and reasonable rate of return to be allowed Tennessee for the purpose of this interim order." We respectfully submit that such conclusion is erroneous in fact and in law, is not supported by substantial evidence of record, and is not

(5427)

supported by adequate findings. Such rate of return, if permitted to stand, is confiscatory, deprives Tennessee of property without due process of law, and would clearly constitute discriminatory and arbitrary and capricious action against Tennessee.

*Returns Recently Allowed
Other Pipeline Companies*

The $6\frac{1}{8}$ percent return allowed Tennessee by the Commission results in a return on its common book equity of only 10.12 percent. Such a return on the common equity ratio of 29.5 percent used by the Commission (see p. 3 of order) is patently unfair, unjust and unreasonable. Such a return, if permitted to stand, will place Tennessee at a decided disadvantage in competing for capital with other regulated industries, including other pipeline companies.

The $6\frac{1}{8}$ percent rate of return allowed Tennessee is to be contrasted with the rates of return allowed in the two most recent rate of return cases decided by the Commission, namely, the *Manufacturers Light*

5428

and Heat Company case (23 F.P.C. 446) issued February 25, 1960, and the *Southern Natural Gas Company* case (Docket G-20509) issued July 8, 1960. In each of these cases, the Commission allowed an over-all rate of return of $6\frac{1}{2}$ percent. In each of these cases, the returns allowed on the respective common equities were *higher* than the return allowed on Tennessee's common equity. In each of these cases, the common equity was *thicker* than the common equity of Tennessee, and, as the Commission has long recognized, a thinner common equity demands a higher rate of return because of the greater risk involved. In

* Throughout this document, the term "common equity" means "common stock book equity."

each of these cases, the *actual* unadjusted imbedded cost of debt was *less* than Tennessee's cost of debt.

Clearly, then, the $6\frac{1}{8}$ percent return which the Commission would allow Tennessee is not commensurate with the returns on investments the Commission itself has just recently allowed other pipeline companies. Clearly, the $6\frac{1}{8}$ percent return allowed Tennessee arbitrarily discriminates against Tennessee.

In the *Manufacturers* case, the Commission allowed a return on common equity of 10.35 percent on an equity ratio of 40.3 percent. If the same rationale were to be applied to Tennessee, it would, because of Tennessee's higher imbedded debt cost, result in an over-all rate of return to Tennessee of 6.77 percent, assuming Tennessee had the *identical* capital structure as that used by the Commission in the *Manufacturers* case. The computation is as follows:

Debt	59.7% at 4.35% = 2.60%
Common Equity	40.3% at 10.35% = 4.17%

Total	6.77%
-------	-------

5429

In the *Southern* case, the Commission allowed a return on common equity of 10.18 percent on a common equity ratio of approximately 36 percent. Assuming the same capital structure for Tennessee as that used by the Commission in the *Southern* case, even the meagre return allowed in the *Southern* case would result in an over-all rate of return of almost $6\frac{1}{2}$ percent for Tennessee. The computation is as follows:

Debt	64.2% at 4.35% = 2.79%
Common Equity	35.8% at 10.18% = 3.64%

Total	6.43%
-------	-------

549

As pointed out above, Manufacturers and Southern were not only allowed higher over-all rates of return and higher returns on their common equity than was Tennessee, but their equity ratios were thicker than that of Tennessee. As the Commission has long recognized, and as shown by the record herein, a lower equity ratio, because of the greater degree of risk involved, demands a higher rate of return (Tr. 167, 171-2). Indeed, as shown by Exhibit 13, pp. 22 and 23, it has been the consistent practice of the Commission to allow higher percentage allowances on thinner equities and lower allowances on thicker equities (Tr. 141).

The evidence shows that on the basis of returns to equity previously allowed by the Commission, a difference in return of about 1.5

5430

percentage points is required for the 10-point difference in equity ratio between 30 percent and 40 percent (Exh. 13, p. 23). Accordingly, assuming that the 10.35 percent return allowed on Manufacturers' equity ratio of 40 percent is reasonable, the return on Tennessee's common equity would have to be approximately 11.9 per cent to give effect to the lower equity ratio (29.5 percent) of Tennessee. As shown by page 4 of the Commission's order here involved, a return on Tennessee's common equity of 11.9 per-

⁵ This is obviously necessary. For instance, if the Columbia System (the parent of Manufacturers) capitalization consisted solely of common stock equity capital, the Commission would not have allowed thereon the 10.35 percent which it allowed on the common stock equity capital amounting to 40 percent of total capital. A uniform percentage allowance on common stock equity capital, regardless of the proportion thereof in the total capitalization, would be completely at odds with regulatory practices and with fundamental principles of finance.

cent would result in an over-all rate of return of almost $6\frac{3}{4}$ percent.⁶

The chart on page 23 of Exhibit 13 is based on adjusted rates of return on common equity to reflect the increase in pure cost of money which has been experienced since the year of the particular Commission decision shown on that chart. But even if no adjustment whatsoever is made to the returns on equity granted by the Commission, the return on Tennessee's common equity would be 11.5 percent, if Tennessee is to be allowed the same return granted to other pipelines on their equity capital, equity ratios considered. A chart prepared in the identical manner as the chart on page 23 of Exhibit 13, but reflecting the unadjusted returns to equity shown in Column 5 of page 22 of Exhibit 13, is attached as Appendix A. The return to equity of 11.5 percent indicated thereon for an equity ratio of 29.5 percent would produce an over-all return to Tennessee of 6.53 percent.

5431

Appendix A also shows that the allowances on common equity of 10.35 percent to Manufacturers and 10.18 percent to Southern are consistent with Commission practice, whereas the allowance of 10.12 percent on the thinner equity of Tennessee materially departs therefrom.

The foregoing, we submit, indicates clearly that the return allowed on Tennessee's common stock equity is not commensurate with the returns recently allowed other pipeline companies, particularly after giving consideration to differences in risks resulting from differences in the thickness of the common equity. Accordingly, by this test

⁶ Even the Commission's Staff did not recommend a rate of return on Tennessee's common equity capital as low as the 10.12 percent allowed by the Commission. The Staff, it will be recalled, recommended, in its brief, a 10.41 percent return on Tennessee's common equity.

(5431)

alone, it is abundantly clear that the Commission's action in allowing Tennessee only a 6 $\frac{1}{8}$ percent over-all return deprives Tennessee of property without due process of law and arbitrarily discriminates against Tennessee.

Returns Earned by Electric Companies

As demonstrated by the record herein (Exh. 14, pp. 4-5) the electric industry, as a whole, has, in recent years, been earning, under rate regulation, a return of about 11 percent on a common equity ratio *thicker* than that of Tennessee. Thus, in 1958, the electric industry earned 10.97 percent on its common equity; in 1957, it earned 10.96 percent; in 1956, it earned 11.04 percent; in 1955, it earned 10.92 percent. Indeed, in only one year (1951) in the past ten years, did the electric industry earn less than 10 percent on its common equity (Exh. 14, p. 5).

The unchallenged and unrefuted evidence of record shows conclusively that electrics are considered by investors as a less risky business than gas pipelines (Tr. 167-9). And this is wholly apart from the fact that electrics generally have thicker common equity ratios than Tennessee (and the pipeline industry generally).

5432

The Commission, in the order here involved, stated (p. 7):

"There is likewise no substantial evidence to support Tennessee's contention that it needs a 14 to 15 percent return on common equity because certain electric utilities have had an average return of almost 11 percent over a period of years. We are not convinced that the selection of electric utilities made by Tennessee presents a proper basis for comparison, or that the differing risks inherent in the two industries

can be measured as Tennessee here proposes. It is significant to note that according to Tennessee's own study, the three largest electric utilities for which data is shown—namely, Consolidated Edison Company of New York, Pacific Gas and Electric Company and Public Service Electric and Gas Company—had earnings on common equity for 1958 of 8.1, 9.7 and 8.6 percent, respectively."

The statement quoted above is replete with error and is contrary to the record. For example, Tennessee does not contend that it needs a 14-15 percent return on common equity. It contends that it needs a return on common equity of approximately 12½ percent. Reference to the record herein (Exh. 34) shows that on Tennessee's corporate capitalization as of March 31, 1960, it was claiming a return on its common equity of 12.52 percent.⁷ Reference to Tennessee's brief herein also shows that Tennessee is claiming only a 12½ percent rate of return on its common equity (See, for example, pp. 11, 12, 27).

Tennessee's claimed return of approximately 12½ percent on its common equity recognizes the fact that a thicker common equity justifies a lower return thereon than the returns of 14-15 percent heretofore allowed Tennessee by the Commission. Thus, on page 27 of its Brief, Tennessee stated:

5433

"Tennessee, however, recognizes that a thicker equity does not require as high a rate of return as does a thinner equity, due to the lesser risk to the common stock investors. In the instant proceeding,

⁷ Exhibit 34 shows an equity ratio of 22.03 percent. This ratio includes as common equity the \$17,463,700 of the 4.5 percent series of convertible second preferred stock outstanding as of March 31, 1960.

Tennessee, as previously shown, has succeeded in thickening its common equity from the range of 20% - 27% in its previous cases to 32.00% as of March 31, 1960. We seek no reward for such action. On the other hand, we do not want to be penalized therefor. Tennessee is requesting in this case only 12.52% return on this thicker equity, as contrasted to the 14% - 15% heretofore requested and received from the Commission. * * *

Moreover, the Commission is in error when it states that "certain" electric utilities have had an average return of almost 11 per cent over a period of years." The fact is, as shown above, that the *average* of the *entire* industry has been about 11 percent on its common equity in recent years—a common equity significantly thicker than that of Tennessee.

The Commission, in the above quotation, points to the fact that three of the electric utilities for which information was shown in a Tennessee exhibit (Exh. 14, p. 4) had returns on equity in 1958 of 8.1, 9.7 and 8.6 percent, respectively. But the exhibit contains information pertaining to 25 electric utilities. Eighteen of those companies earned more than 11 percent on their common equities—common equities which in every single case were also *thicker* than Tennessee's. We submit that selecting the three companies which had the lowest returns on common equity is arbitrary and does not constitute a valid or fair comparison under the principles enunciated by the Supreme Court in the *Bluefield* and *Hope* cases, *infra*. Tennessee is legally entitled to earnings commensurate with earnings in other enterprises having corresponding risks. This should not, and cannot legally, be interpreted as meaning that Tennessee

* Emphasis supplied.

5434

is entitled to earnings commensurate with the lowest rate of earnings being earned by three selected companies.

The Commission questions the propriety of selecting the electric industry as a basis for comparison, and also questions (in the quotation above) whether the differing risks inherent in the electric and pipeline industries can be measured "as Tennessee here proposes." But the record contains specific, unrefuted, and unchallenged expert testimony by one of the leading investment bankers in the country that electricies are regarded by investors as being comparable with the natural gas industry, except that the *natural gas industry is regarded as having somewhat greater risks than the electric industry* (Tr. 167-9). Indeed, it is a matter of common everyday knowledge that electricies are considered one of the least risky and most stable utilities in the country. The comparison with the electric industry cannot arbitrarily be dismissed or brushed aside, we respectfully submit, simply because such comparison, by every reasonable standard, demonstrates that the return allowed to Tennessee by the Commission is too low.

Moreover, the return of 10.12 percent allowed Tennessee on its common equity is not only unsupported by the record and by appropriate findings, but flies directly in the face of the record. *It is lower than that actually being earned by the electric utility industry. It is lower than the average earned since 1951 by the 10 major pipelines in the country*. (See Exh. 22). Indeed, *it is substantially lower than the average (12.4%) earned in the past several years on common equity by the entire natural gas industry regulated by the Commission* (Tr. 1499; See Statistics of Natural Gas Companies, 1958 edition, p. XII, issued by Federal Power Commission).

The foregoing further serves to show that the return allowed Tennessee on its common equity deprives it of property without due process of law, is contrary to the evidence of record, is unsupported by the record and by appropriate findings of fact in violation of Section 8(b) of the Administrative Procedure Act (5 U.S.C. 1007 (b)), and is arbitrary and capricious.

Use of Earnings-Price Ratios

The Commission (on page 5 of its order) refers to various earnings-price ratios for Tennessee and the pipeline industry generally and states that earnings-price ratios "may properly be used with judgment, together with other factors," in determining a reasonable allowance on common equity. The Commission concludes that Tennessee's earnings-price ratios over the past 12 years compare favorably with those of the other major pipeline companies, and are generally equal to or lower than those of the industry as a whole. Such a conclusion, we respectfully submit, in no way supports the propriety of the 10.12 percent return allowed Tennessee on its equity. Moreover, such conclusion is unsupported by appropriate findings indicating the use to which the earnings-price ratios were put in order to arrive at the 10.12 percent return on common equity.

The mischievous—indeed, the extremely dangerous and erroneous—aspect of the blind and indiscriminate use of earnings-price ratios in the natural gas pipeline field is the apparent assumption that such ratios are a direct measure of a fair and reasonable return on the *book value* of the common equity. In all the experience of Mr. L. E. Katzenbach, a general

5436

partner of White, Weld & Company,² he has never encountered a single responsible investment officer of any trust company, insurance company, mutual fund, pension fund, or any other manager of investment funds, who employed any such philosophy (Tr. 1446-7).

The fact is that earnings-price ratios do *not* measure what it takes in the form of earnings on *book value*, as distinguished from market value, to attract equity capital. This fact can be demonstrated by a simple example. Thus, the stocks of most natural-gas transmission and distribution companies and of most electric light and power companies sell at prices materially in excess of book value (Tr. 1447). Assume, for example, that a company's common stock sells at a price of \$34.00, that its most recently reported earnings were \$1.70 a share, and its book value \$17.00 a share. In this example, the company is earning 10% on its book value and its stock is selling at an earnings-price ratio of 5 percent. The Commission's earnings-price ratio theory of fixing return on common equity erroneously assumes that the investor who pays \$34.00 per share, thereby establishing an earnings-price ratio of 5 percent, is satisfied with a 5 percent rate of return on *book value*, which return amounts to only about 2½ percent on his investment. This means that although the company earned \$1.70 a share last year, the investor would be content if the company earned 5 percent on its \$17.00 book value, or 85¢ per share, in the future. Obviously, investors are not so lacking in common sense.

² White, Weld & Company, during the past five years, has acted as the managing underwriter or as the co-manager of public offerings of corporate securities aggregating more than three billion dollars. It is generally considered to have a broader familiarity with, and experience in, the natural-gas pipeline field than any other firm in the country (Tr. 151-2).

Conclusive proof of the fallacious nature of earnings-price ratios is readily apparent in this record. Thus, the average earnings-price ratios of the 10 natural gas companies used in the Staff's exhibit was, for the years 1953 to 1958, 6.58 percent (Exh. 21, p. 37). The *actual* earnings, however, of the 10 companies on their common stock book equities for that period was 15.6 percent (Exh. 22). In other words, if earnings-price ratios are an actual measure of the "cost" of equity capital, the Commission has been more than 100 percent wrong in its previous allowances on equity capital. The plain answer is that the earnings on the equities—earnings which have been the basis of the sales of millions of dollars of common stocks—are sound and that the use of earnings-price ratios as a measure of the "cost" of equity is basically wrong.

Exhibit 21, pp. 11-15, shows that in very recent years the bonds and debentures of natural-gas pipeline companies have been selling to yield in the neighborhood of 5.0-6.0 percent. Corporate bonds generally had a yield of 4.67 percent in 1959 and U.S. Government long-term securities had a yield of 4.07 percent in the same year. Moody's Aaa bonds had a yield of 4.49 percent in 1959. On the other hand, the dividend yield on Standard and Poor's 500 common stocks was 3.23 percent in 1959, while the yield on the 10 natural gas common stocks selected by the Staff ranged from 2.5 percent to 4.9 percent in 1959 (Tr. 1097-9; Exh. 21, pp. 23-32). This is proof positive that natural gas common stocks are not purchased for current yields and earnings, as the Commission erroneously assumed.

Even earnings-price ratios, the record shows, are less, in many cases, than the yields on Aaa bonds. Thus, the aver-

age earnings-price ratio in 1959 on Tennessee's common stock was 5.0 percent. During the

5438

month of July, 1959, the earnings-price ratio on Tennessee's common stock was 4.5 percent (Exh. 23). The earnings-price ratios on common stocks of other natural-gas pipeline companies were similarly low. Thus, for the 12 months ended September 30, 1959, the earnings-price ratio on El Paso's and Southern Natural's common stock was 5.1 percent. The composite earnings-price ratio of the ten larger natural gas pipeline stocks was 6.0 percent (Exh. 21, p. 38). The highest earnings-price ratio on Tennessee common stock was 8.5 percent in 1948. In only three years since then did the earnings-price ratio exceed 7 percent, namely, 1949, 1951 and 1953. In every other year, the earnings-price ratio was less than 7 percent. The average for the years 1948-1959 was 6.5 percent (Exh. 21, p. 29).

Still further evidence of the treacherous nature of earnings-price ratios for use in determining proper allowances for common stock equity may be found by comparing earnings-price ratios of electric utilities with the actual earnings of such utilities. The earnings-price ratios for Moody's 24 electric utility common stocks for the years 1952 to 1958, inclusive, was 6.61 percent (Exh. 13, p. 15). However, the earnings on common equity of electric utilities in the United States, according to Statistics of Electric Utilities for 1958, published by the Federal Power Commission, averaged 10.9 percent (Table 5, page XII). This disparity clearly shows that earnings-price ratios are not, and cannot be, used as a basis for the fixing of electric utility rates.

Dr. Shaffner, the Staff witness, stated (Tr. 1013) that earnings-price ratios should "be used with judgment and discretion," and that they "should not be used on a spot

basis, or on a basis of transitory and untypical conditions." In times like the recent past, Dr. Shaffner testified,

5439

"they should be considered as the minimum return which it takes to attract equity capital, as a floor, so to speak." Mr. Katzenbach, on the other hand, categorically stated (Tr. 1451) that they should not be used at all "because the premise that earnings-price ratios are indicative of the rates of return on common stock equity—that is to say, book value—necessary to attract capital is mistaken."

The 1958 report of the Committee on Corporate Finance of the National Association of Railroad and Utilities Commissioners (NARUC) clearly supports Mr. Katzenbach. Thus, that report categorically states that "the use of low current earnings-price and current dividend price ratios are meaningless as a measure of investor expectations, and, therefore, inadequate as a measure of the cost of common stock equity" (Tr. 1114-5).¹⁰

The foregoing, we submit, demonstrates that the Commission's reliance on earnings-price ratios to support the return allowed on Tennessee's book equity of 10.12 percent is misplaced and is unsupported by the record herein and by appropriate findings of fact. Its order is, therefore, in violation of Section 8(b) of the Administrative Procedure Act (5 U.S.C. 1007(b)).

Coverages

The Commission (p. 7 of order) observed that there is "no substantial evidence to show that such coverage ratios must be maintained at levels

¹⁰ In this connection the study of the West Virginia Commission witness, referred to in the order here involved, was confined to two brief periods, namely, the month of May, 1953, and a four-week period in 1960, and is, therefore, completely unreliable either for the purpose of determining "cost" of common stock capital or as corroborating the "cost" arrived at by the Commission.

5440

comparable to those of 1954 and prior years, nor is there evidence of comparability with other companies and industries to show that the quality of Tennessee's senior securities will suffer in the market place if Tennessee is not on the 7 percent rate of return which it seeks." The Commission is in error.

The record contains unrefuted and unchallenged testimony on the matter of coverage ratios by an eminently qualified expert witness, Mr. Katzenbach (Tr. 151-2; Tr. 160-4). Mr. Katzenbach, after discussing the decline which has taken place in Tennessee's coverage ratios, testified (Tr. 163-4)

"I know from first-hand experience in dealings and negotiations with investment officers of institutions which represent the market for, and from whom the funds must come for the new issues of debt securities, that the maintenance of adequate margins of coverage of interest requirements and sinking fund payments is a matter of prime importance and that if these margins of coverage are allowed to deteriorate further, the result would be a definite downgrading in the investment quality of Tennessee's securities in the eyes of investors.

"This can only lead to a situation where Tennessee is placed at a disadvantage with respect to the terms upon which it can obtain additional capital for its future expansion. The figures and computations shown on pages 2 and 3 of my exhibit [Exh. 14] may seem a trifle theoretical but the problem is not a theoretical one by any means. The figures and computations merely serve to demonstrate that a 7% return under present conditions is no more than sufficient to maintain the standard of financial soundness which Tennessee was able to present to investors in past years."

(5440)

The foregoing, we submit, shows clearly that the Commission's conclusions as regards coverage ratios is contrary to the unrefuted and unchallenged evidence of record. *Thickening of Tennessee's Equity*

As shown by page 14 of Exhibit 13, Tennessee's equity has varied from 27.75 percent in 1946 to 19.80 percent in 1954. Recently, however,

5441

Tennessee has succeeded in thickening its equity to a ratio of approximately 30 percent. That the thickening of equity is desirable is attested to by the Commission's decision in the *El Paso* case (Opinion 278) wherein the Commission, in allowing *El Paso* a return on equity of 14.4%, observed (*mimeo.*, p. 38) that such return "should permit and encourage it to make further improvement in its capital structure." In the last decided Tennessee rate case (Docket G-5259) wherein Tennessee was allowed a return on equity of 13.71%, it was observed (18 F.P.C. at p. 441—decision issued October 17, 1957) that Tennessee's common equity ratio, which was 21.80 percent as of the end of 1955 "should be improved."

In the *Manufacturers* case, *supra*, the Commission observed (23 F.P.C. at p. 448) that Columbia (which does all the financing for Manufacturers, its subsidiary) "has commendably continued its practice of maintaining a conservative capital structure with no undue thinning of the equity." The Commission further observed that "the public interest would be best served by encouraging this practice."

And in the *Southern* case, *supra*, the Commission pointed to the fact that:

"Southern has maintained a conservative capital structure without undue thinning of its equity, where-

(5442)

as the industry as a whole has frequently resorted to high leverage financing in order to maintain profit levels, and we have consistently held the public interest is best served by allowing a return on equity which encourages such conservative financial structures."

But does the 6½ percent return allowed Tennessee encourage Tennessee to continue its recent practice of thickening its equity? Patently not. Thus, if Tennessee were to increase its common equity ratio to 40% (the common equity ratio of Manufacturers) *the resulting return*

5442

on Tennessee's equity ratio of 40 percent would be only 8.61 per cent. The computation is as follows:

Debt and Preferred Stock	60% × 4.45% ¹¹	= 2.67 %
Common Equity	40% × 8.61%	= 3.445%
Total		6.125%

If Tennessee were to increase its common equity ratio to the level of Southern's, namely, 36%, the 6½ percent return allowed Tennessee would result in a return on such thicker equity ratio of only 9.1%. The computation is as follows:

Debt and Preferred Stock	64% × 4.45%	= 2.85 %
Common Equity	36% × 9.10%	= 3.275%
Total		6.125%

The foregoing, we submit, makes crystal clear the fact that the return allowed Tennessee discourages the very thickening of the equity which the Commission seeks to

¹¹ Weighted average cost of Tennessee's debt and preferred stock capital (derived from pp. 3 and 4 of order of August 9, 1960).

encourage. The foregoing also serves to demonstrate still further the confiscatory, discriminatory and arbitrary nature of the Commission's rate of return allowance to Tennessee.

Minimum Bill Provision

The Commission found (p. 6 of order) that "Tennessee has a relatively low risk in connection with the recovery of its cost of service by reason of the minimum bill provisions of its rate schedules guaranteeing at least 69.5 percent of its estimated revenues from jurisdictional business." Such finding is erroneous, insofar as it implies that whatever

5443

lesser risk exists should be reflected in a lower return on Tennessee's common equity.

In the first place, there is no evidence in the record as to minimum bill provisions of other pipeline companies and of electric utilities. Accordingly, the relative risk cannot be measured. Secondly, the Staff witness who testified as to the minimum bill provision admitted that he did not know whether the minimum revenues would even cover fixed and operating expenses (Tr. 1227). Finally, to the extent that the minimum bill provision is a factor considered by investors, it is already reflected in the return requirement on common equity capital and in the interest rates and dividend rates on senior securities (Tr. 1159-60).

Gas Reserves

The Commission also found (p. 6 of order) that "Tennessee's position is further strengthened by its rapidly increasing gas reserves, these reserves having increased 63 percent since 1950 as compared to an increase of 36 percent for the nation's reserves for the same period." This finding, however, is misleading. Patently, gas reserve figures are meaningless unless such reserve figures are

compared with requirements. The record shows, in this regard, that the reserve life index of Tennessee gas reserves has decreased from 34 years in 1947 to 24 years in 1956. (Item A, pp. 3463-7).

Test of Bluefield and Hope Cases

In the *Bluefield* case (262 U.S. 679) the Supreme Court stated the test of a fair rate of return as follows:

5444

"A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties."

In the *Hope* case (320 U.S. 591) the Supreme Court stated:

"... the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and attract capital."

The 6 $\frac{1}{8}$ percent over-all return (and the 10.12 percent return on common book equity) clearly do not meet the test of the *Bluefield* and *Hope* cases. The return allowed Tennessee will *not* enable it to earn a return on its property "equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties." This is apparent from the fact that, as previously shown, the return allowed Ten-

(5444)

nessee is substantially less than that being earned by, and being allowed to, other business undertakings attended by corresponding risks and uncertainties.

Tennessee claims no vested right in the 14-15 percent returns heretofore consistently allowed to it by this Commission. But Tennessee, as well as the tens of thousands of investors in its securities, have the right to expect the Commission to protect the integrity of the investments they have made in Tennessee. Those investors have the right to expect that the increased cost of debt incurred in expanding the system to meet the needs for natural gas would be offset by appropriate allowances in the rate of return. Those investors have the right to expect that they will be treated as fairly as investors in other pipeline companies and other

5445

regulated companies. Those investors had the right to expect consistent regulatory policy as to all companies. Those investors also had the right to expect that in a period of time when practically all costs, including the cost of money, have gone up, the Commission would not arbitrarily reduce earnings on their common book equity by approximately one-third.

"Financial Integrity"

The Commission concludes (p. 7) that the rate of return allowed Tennessee is sufficient to "preserve" Tennessee's "financial integrity." Such conclusion is not supported by substantial evidence and adequate findings. A finding of financial integrity cannot be made in a vacuum. Yet, the Commission has done precisely this. The Commission has deferred for later hearing and determination the rate of return applicable to Tennessee's production properties, stating (at p. 7) that "final determination of the proper rate of return on production properties cannot be made

at this time, but will be made upon conclusion of the next phase of the proceeding." It is thus clear that the Commission cannot, on the basis of the present record, determine whether the $6\frac{1}{8}$ percent over-all rate of return which it has allowed is fair and reasonable and sufficient to preserve the financial integrity of Tennessee (See *El Paso Natural Gas Company v. Federal Power Commission*, No. 18022, 5th Cir. enit. Decided August 2, 1960). For example, if the Commission were to find, as we believe it must, after completing the next phase of the proceeding, that Tennessee is entitled to a higher rate of return than $6\frac{1}{8}$ percent on its production properties, how could Tennessee recover such additional return retroactively after having made refunds to its customers on the basis of a $6\frac{1}{8}$ percent return pursuant to the interim order?

5446

There are other important issues not yet fully heard which vitally affect the question of whether the return of $6\frac{1}{8}$ percent is adequate to protect the financial integrity of the company. For example, until the Commission has fully heard and decided the depreciation issue in this case, it cannot make an appropriate cash flow study to determine whether Tennessee will have sufficient cash to pay interest on its bonds, dividends on its preferred stock and meet the sinking fund requirements on its securities.

The Commission cannot, therefore, now make the finding that the rate of return allowed, Tennessee will "preserve its financial integrity." Moreover, it is difficult to perceive how a rate of return lower than the returns being earned by, and being allowed to, more secure regulated business enterprises can preserve the financial integrity of Tennessee, and enable it to attract capital on comparatively favorable terms and conditions.

(5446)

Other Errors

In arriving at the rate of return allowed to Tennessee, the Commission utilized a consolidated capitalization which reflected the capitalization ratios and cost of capital of Tennessee and its subsidiaries as of February 29, 1960 (p. 3). In so doing, the Commission erred in failing to reflect and take into consideration the financing of Midwestern Gas Transmission Company which has been consummated pursuant to a plan heretofore submitted to, and approved by, the Commission. As the Commission was aware at the time it issued its order herein, Midwestern issued and sold \$60,000,000 of first mortgage bonds at a coupon rate of $5\frac{3}{4}$ percent

5447

with a net cost to the company of 5.92 percent.¹² Yet, the Commission used a capitalization reflecting the former cost of debt capital to Midwestern which consisted of a bank loan of \$35,000,000 with a cost of 5.07 percent, which loan has been retired.

The Commission further erred in refusing to treat as common equity the \$19,264,000 of 4.50 percent series of convertible second preferred stock which, as of February 29, 1960, had not been converted into common stock (p. 4 of order). In so doing the Commission ignored the rapid rate at which conversion is taking place and also ignored the fact that the very purpose of issuing convertible second preferred stock is to thicken the equity in the most economical manner. The rapidity at which conversion is taking place is evidenced by the fact that by March 31, 1960, the amount of the 4.50 percent series of convertible second preferred stock which remained to be converted was \$17,463,700 (Tr. 1505); during April, 1960, an additional

¹² This matter was referred to in Tennessee's brief in this proceeding at page 6.

\$1,768,500 was converted, leaving less than \$16,000,000 outstanding as of the end of that month (Tr. 1505); and by the end of July 31, 1960, only \$13,262,200 remained to be converted.

These facts must appropriately be recognized and given full effect, particularly in a case such as this where rates are being fixed for the future. In cognate circumstances the Commission gave effect to imminent future changes in the cost of capital of Southern Natural Gas Company in its interim order issued July 8, 1960 at Docket G-20509, wherein the Commission stated (at p. 4):

5448

" * * * The *pro forma* adjustment of the weighted average cost of debt as of December 31, 1959, to reflect the retirement of the bank notes and the issuance of long-term debt securities to replace them is proper in this case where we are determining rates for the future and where the funding of such loans in the very near future is reasonably to be expected and such funding is consistent with good practice. We therefore find Southern's cost of debt capital to be 4.45 percent, as determined by both Southern and staff."

The Commission's refusal to accord similar treatment to Tennessee is but another example of the discriminatory character of the Commission's order.

We respectfully urge the Commission, in the light of all of the foregoing, to reconsider its order herein of August 9, 1960, and upon such reconsideration to allow the 7 percent rate of return claimed herein by Tennessee.

II

Interim Rate Reductions and Refunds

The order here involved disallows the rates presently in effect, permits Tennessee to file substitute rates, effective

(5448)

as of April 5, 1960, reflecting a 6 1/8 percent rate of return, and requires Tennessee to refund to its jurisdictional customers the difference between the presently-effective rates and the substitute rates. The order also requires Tennessee to accompany its substitute filing "with supporting cost of service and allocation data, to be computed and presented in the same form and manner as continued in its exhibits heretofore offered by it in this proceeding, revised only to reflect a 6 1/8 percent rate of return and Federal income taxes associated therewith." (p. 10 of order).

The Commission's disallowance of the presently-effective rates and its requirement that reduced rates be filed and refunds made is unlawful

5449

and inequitable. But even assuming, *arguendo* that the Commission has the legal authority to require interim rate reductions and refunds, such requirement, in the circumstances of this case, constitutes a flagrant abuse of discretion.

The Commission points out in its order (p. 8) that Tennessee contends that the interim order procedure is unlawful and inequitable unless the Commission makes final disposition of the issue of cost-allocation and rate design at the same time it determines the proper rate of return. "since Tennessee may not be able to recover its cost of service should the Commission decide these issues in such a way that Tennessee would have to make refunds in certain zones where its rates are found to be too high but could not recover revenues retroactively in those zones where it has charged less than the finally determined cost of service."

The Commission then dismisses this contention by quoting with approval from its order in the *Southern* case wherein it stated that:

"Should Southern suffer legal injury by reason of the Commission's final order in the second phase of this proceeding, it may seek judicial review. It cannot, however, be heard to complain of an order which fixes a proper rate of return and looks only to the establishment of interim rate levels based on such proper return and which in all other respects are based on the methods and procedures employed by Southern in making its rate filing, including its own allocation and rate design methods."

But Tennessee files rates. It does not file cost allocations or rates of return. To be sure, cost allocations and claimed rates of return are submitted with rate filings. But it is the level of the rates which is significant from the rate-making standpoint. If the level of a particular rate is reasonable judged by such method of cost allocation as may be ultimately adopted by the Commission, it makes no difference

5450

that the particular rate was predicated on a different method of allocation. Stated differently, until and unless the Commission determines the method of allocation to be used for allocating costs among the six rate zones on the Tennessee system, it does not know, and cannot make the finding, that the rates in each and every zone are unjust, unreasonable, or unduly discriminatory.

Section 4(e) of the Natural Gas Act provides that "after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective." Here, it is to be noted, full hearings have not been held or completed as to the reasonableness of the interim rates which the Commission requires Tennessee to

(5450)

file. One of the untried issues is the question of what rate of return shall be allowed on Tennessee's production (well-mouth) properties. The Commission's order specifically defers this issue for later hearing. Until this issue is finally heard and disposed of, the Commission has no way of knowing whether the 6 $\frac{1}{8}$ percent over-all rate of return which it has allowed in its interim order is adequate for Tennessee. As pointed out elsewhere herein, if the Commission should later determine that Tennessee is entitled to a higher rate of return than 6 $\frac{1}{8}$ percent on its production properties, Tennessee will be unable to recover such additional return. The Commission's order, therefore, deprives Tennessee of due process of law in failing to afford Tennessee a full hearing on this vital issue *before* entering its order reducing rates.

Section 5(a) provides that "Whenever the Commission, *after hearing* * * * *shall find* that any rate * * * is unjust, unreasonable;

5451

unduly discriminatory, or preferential, the Commission shall *determine* the just and reasonable rate * * * to be thereafter observed and in force, and *shall fix* the same by order: * * *." While the interim order purports to find that Tennessee's filed rates are unjust and unreasonable, the Commission cannot lawfully make a finding as to the reasonableness of the specific rates filed for each zone because it has not yet decided the allocation issue. This is so for the reason that the Commission has refused to determine what portions of the over-all cost of service (as reduced by the lowering of the rate of return from 7 percent to 6 $\frac{1}{8}$ percent) is properly allocable to each of Tennessee's six zones. Such reduced cost of service must be *allocated* to each of the separate zones and compared with the revenues yielded by the filed rates in each zone before the Commission can possibly know whether the filed rates are

higher or lower than the cost of service applicable to each zone. Such determination must be made by the Commission—it cannot be lawfully delegated to Tennessee—before the Commission can definitively find, as required by the statute, that the filed rates are too high, too low, or unduly discriminatory in any particular zone. It is, therefore, clear that the Commission's purported general finding of unreasonableness of Tennessee's filed rates is arbitrary, capricious and without warrant in law or fact.

By the same token, the Commission cannot lawfully *prescribe* rates for the various zones, as required by the provisions of the Natural Gas Act quoted above, until it first determines the method to be used for allocating the cost of service among Tennessee's rate zones and services. Indeed, the Commission's order wholly failed to enter the

5452

necessary statutory finding that the rates which it requires Tennessee to file are just and reasonable interim rates. It failed to make such finding because it could not do so since it has refused to adjudicate the issue of zone allocation.

The Commission's order requires Tennessee, under pain of forfeiting its entire rate increase, to file reduced rates based upon Tennessee's proposed method of cost allocation. Since the cost allocation issue is one of the most controversial issues in this case and had not yet been decided, the Commission has placed Tennessee in the precarious position of making refunds and charging interim rates to its customers at its peril pending a later decision by the Commission on the question of whether such refunds and interim rates are in fact just and reasonable. If the Commission should later decide that a method of allocation should be used other than the one used by Tennessee, then Tennessee may not be able to recover its total

cost of service, including even the meagre rate of return here allowed.

We respectfully submit that such a "heads-we-win-tails-you-lose" method of rate making is an abuse of discretion and does not measure up to the standards of fair play or due process of law.

As stated above, the allocation issue was fully tried over a period of three years, has been fully briefed, and has been ripe for decision for more than four months. What possible justification can there be under the circumstances for refusing to omit the intermediate decision and decide this issue before ordering Tennessee to reduce its rates. Surely, Tennessee should not be required to proceed in total darkness as to the Commission's views regarding allocation of costs—views which

5453

must be known before a determination can be made as to which classes of customers in which zones are entitled to what rate reductions, if any. Under what theory of law, logic, or fair play should Tennessee be required to proceed at its own peril to make refunds and reduce rates under one method of allocation at the risk of being later told that a different method of allocation should have been used and that Tennessee must forfeit a large part of its cost of service because it made a wrong guess as to the allocation method which would eventually be adopted by the Commission.

Where cost allocation is not an issue in a case or where a future order of the Commission cannot operate retroactively in such a manner as to jeopardize the ability of a company to recover its cost of service, an interim rate reduction may be appropriate. That was the situation in the cases cited and relied upon by the Commission in the *Southern* order, *supra*. But cost allocation is an issue pending decision now by the Presiding Examiner in Docket G-11980. The Presiding Examiner has ruled that what

ever method of cost allocation is finally adopted in Docket G-11980 will be applicable in the instant docket (Tr. 453-6).

As stated above, if Tennessee is required now to reduce its rates and to make refund, it will be placed in jeopardy of not being able to recover its cost of service if the method of allocation ultimately selected allocates more cost of service to a particular rate zone than the revenues produced by the interim rates. It is no answer, we submit, to state that

5454

Tennessee may seek judicial review if it should suffer legal injury by reason of the Commission's final order in the *second phase* of this proceeding. It is no answer because it is the *instant* order which places Tennessee in jeopardy of not being able to recover its cost of service if refunds have already been made and the reduced rates have been collected.

Assuming *arguendo*, however, that the order here involved is legally appropriate from the statutory standpoint, we respectfully submit that the order, nevertheless, is invalid as constituting an abuse of discretion. As the Commission knows, Tennessee's customers are fully protected by Tennessee's undertaking in this docket to make refunds, with interest at 7 percent, of excess charges collected. As the Commission also knows, the well-being of a company depends on its ability to recover its cost of service. Why, we respectfully ask, should the Commission jeopardize the financial well-being of a company by an interim order such as is involved here? What emergency has arisen that requires the Commission to place Tennessee in such jeopardy? The desire for expedition of rate cases is, of course, commendable, and we fully support

¹³ As pointed out in our Memorandum (pp. 7-8) in this docket filed with the Commission on June 13, 1960, the exposure to which Tennessee is subjected by the instant order involves several millions of dollars.

(5454)

and likewise desire expedition. But the desire for haste must give way to the need to protect the rights and property of others.

Basic fairness, we submit, dictates that the Commission not require rate reductions and refunds until the allocation issue is also decided. This is particularly so in view of the fact that the Commission has not heretofore prescribed a method of allocation for use on the Tennessee system. We, therefore, urge the Commission, upon rehearing, to delete any provision requiring rate reductions and refunds until such

5455

time as the entire rate of return issue is fully heard and the allocation issue is finally decided.

WHEREFORE, in view of all the foregoing, it is respectfully urged that the Commission grant rehearing of its order issued August 9, 1960, as requested herein.

Respectfully submitted,

TENNESSEE GAS TRANSMISSION COMPANY

By /s/ HARRY S. LITTMAN

By /s/ JACK WERNER

Its Attorneys

William C. Braden, Jr.

B. J. Williamson

Tennessee Building

Houston 1, Texas

Harry S. Littman

Jack Werner

Harold L. Talisman

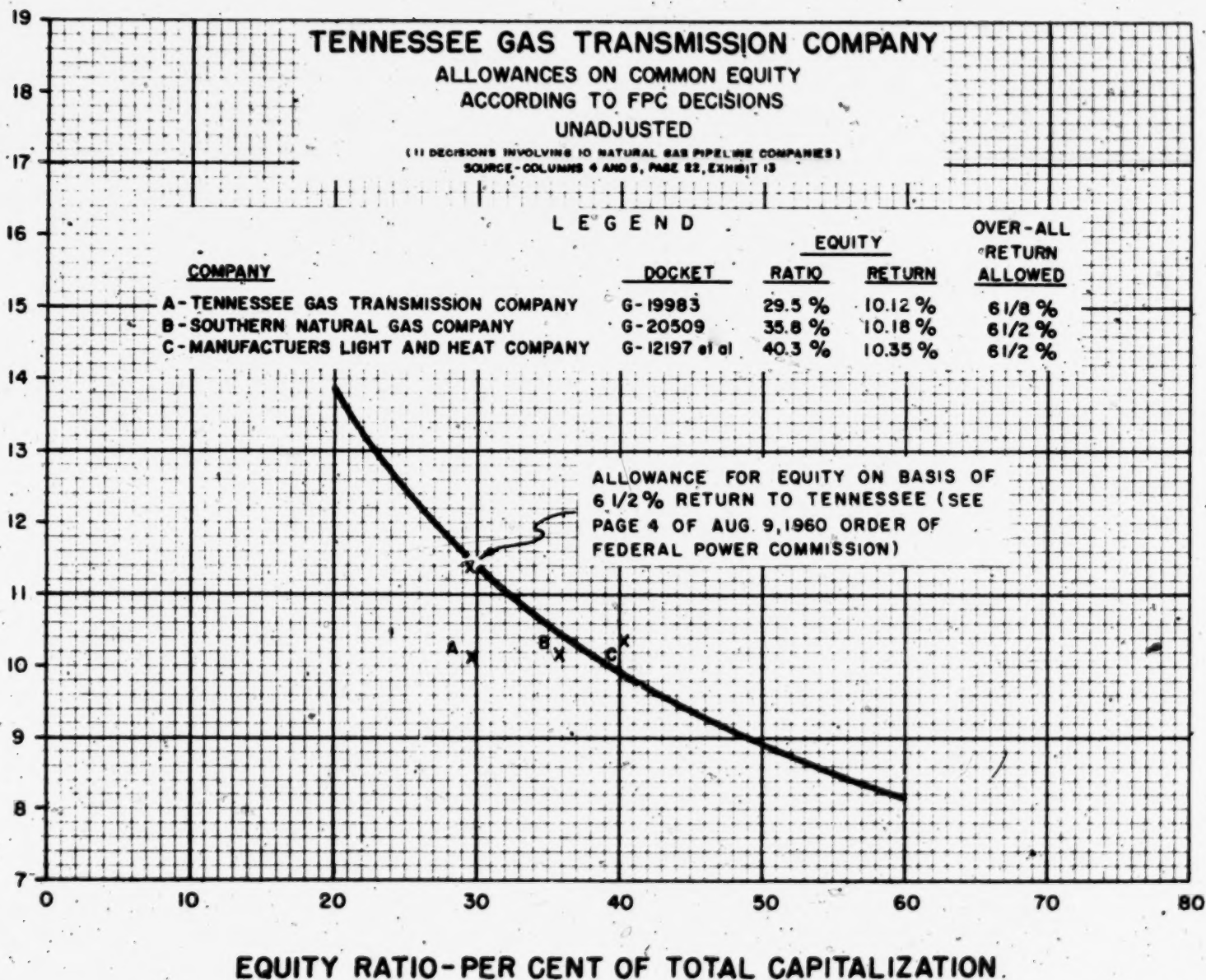
317 Wyatt Building

Washington 5, D. C.

*Attorneys for Tennessee Gas
Transmission Company*

August 29, 1960.

5457



5470

(Received Aug. 30, 1960)

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Docket No. G-19983

In the Matter of

TENNESSEE GAS TRANSMISSION COMPANY

Joint Application and Petition for Rehearing on Behalf of the Manufacturers Light and Heat Company, the Ohio Fuel Gas Company and United Fuel Gas Company So That the Commission Will Reconsider and Modify Its Order Issued August 9, 1960, Insofar As It Pertains to Interim Refunds.

Pursuant to Section 19 of the Natural Gas Act and Commission Rule 1.34; The Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company ("Petitioners"), being aggrieved parties, hereby apply and petition for rehearing and request that the Commission reconsider and modify its order issued August 9, 1960, in Docket No. G-19983.

Petitioners urge that the Commission abrogate said order insofar as it requires Tennessee to make interim refunds to its jurisdictional customers effective as of April 5, 1960, prior to the final determination of *all* of the inseparable issues involved in the proceeding.

Petitioners urge this relief for the following reasons:

I. GROUNDS RELIED UPON BY PETITIONERS

1. *The Commission cannot reduce the rates charged by Tennessee in Zones 1, 5 and 6 without depriving Petitioners of rights created by Section 4 of the Natural Gas Act and Commission Rules 2.4 and 2.52.*

5471

Petitioners are substantial customers of Tennessee Gas Transmission Company ("Tennessee") in Tennessee's Rate Zones 2, 3 and 4. Since 1947 Petitioners have been subjected to periodic increases in Tennessee's rates which have been *disproportionately* higher in Rate Zones 2, 3 and 4 than in the other rate zones of Tennessee. Petitioners have complained formally to the Commission that they have been subjected to undue rate discrimination by reason of Tennessee's undercharges to customers in its Zones 1, 5 and 6. The Commission has for many years recognized the existence of the issue of unlawful rates between zones and set Docket No. G-11980 as the proceeding in which to determine the basic controversy as to the principles and methods to be applied towards allocation of costs among zones and classes of service within the zones.*

In this context on October 5, 1959, Tennessee filed increased rates in *all* of its Zones 1 through 6, which rates are the subject of this proceeding, Docket No. G-19983.

Petitioners submit that this voluntary filing by Tennessee for higher rates in Zones 1, 5 and 6 created direct, real and substantial rights, interests and benefits to Petitioners and other customers of Tennessee in Rate Zones 2, 3 and 4. Petitioners submit that their legal rights so created are adversely affected by the Commission's interim refund order issued August 9, 1960. This stems, in part, from three undeniable premises; namely,

5472

1. Petitioners' have before the Commission a long-standing charge that Tennessee has violated Section 4(b) of the Natural Gas Act by subjecting Petitioners in Zones 2, 3

* See Docket No. G-5259, orders issued October 6, 1955 and September 5, 1957; Docket No. G-11980, order issued April 30, 1959.

and 4 to undue rate discrimination, prejudice and disadvantage in favor of Tennessee's customers in other Rate Zones and classes of customers;

2. Section 5(a) of the Natural Gas Act specifically deprives the Commission of the power to order Tennessee to increase any of its filed rates; and

3. As one essential step in the rate making process, the Commission is determining the rates for each of the six Rate Zones of Tennessee on the basis of assigning portions of Tennessee's total cost of service to those customers responsible therefor.

Thus, the Commission's interim refund order prejudged and predetermined arbitrarily that the rates charged by Tennessee in its Zones 1, 5 and 6, pursuant to the Commission's order issued April 29, 1960, are *not* too low. Such action prejudices Petitioners, who have contended for years that said rates are too low, and once the rates have been reduced the Commission lacks the power subsequently to require them to be increased.

Petitioners' position is supported by Commission's Rules 2.4 (c)(2) and (3) and 2.52. Said Rules recognize that not only are rate *increases* suspendable, but also rate *reductions* and *discriminatory changes* are suspendable when filed by regulated companies. It is submitted that this rule

5473

recognizes the right of customers which are being subjected to undue rate prejudice or disadvantage to have "full hearings" under Section 4(e) of the Natural Gas Act before the Commission may order rate *reductions* to other customers which are being granted undue rate preferences or advantages in violation of Section 4(b) of the Natural Gas

(5473)

Act. There can be no other explanation for the necessity or propriety of suspending rate reductions.

2. *Petitioners have been denied the opportunity to adduce evidence on cost allocation herein, which would support their contention that Tennessee's rates in Zones 1, 5 and 6 are too low and should not be reduced.*

At T. 302, 1235-1241, the Presiding Examiner ruled that he would not receive rebuttal evidence on the issue of cost allocation in Docket No. G-19983. The Examiner has only received evidence which follows the contested manner of cost allocation proposed by Tennessee. It is submitted that since cost allocation is an essential step in the rate making process herein, the Commission lacks the authority to reduce Tennessee's rates in Zones 1, 5 and 6 and deprives petitioners of their right to "full hearings" under Section 4(e) of the Natural Gas Act and Section 7(c) of the Administrative Procedure Act.

3. *The Commission's interim refund order aggravates and complicates the rate controversy among the parties so as to be an abuse of the administrative process.*

As aforesaid, the Commission has set Docket No. G-11980 as the proceeding in which it will determine the prin-

5474

ciples and methods of cost allocation as a necessary step in determining the just and reasonableness of Tennessee's rates. It is submitted that the Commission's interim refund order short-circuits the procedure it has previously set as the framework for deciding the controversy. In addition, Petitioners' rights under Section 19 of the Natural Gas Act insofar as Docket No. G-11980 is concerned would be prejudiced by said interim refund order in Docket No. G-11983.

4. The Commission's interim refund order herein erroneously relies upon its order issued July 8, 1960, in *Southern Natural Gas Co., Docket No. G-20509*, as a precedent and in turn sets an improper precedent contrary to the scheme of the Natural Gas Act.

In its order issued in *Southern Natural, supra*, the Commission relied upon several administrative and judicial precedents. Petitioners submit that all of these so-called precedents are not apposite or are themselves contrary to law.

Petitioners submit that the long history of unresolved charges of undue rate discrimination distinguishes the instant case from *Southern Natural, supra*. All the other citations relied upon by the Commission are distinguishable from the Tennessee situation in that in those cases:

(1) The interim orders in those cases were "final" in the sense that they were not susceptible to retroactive adjustment by a subsequent order;

(2) No allocation issues were involved;

(3) The parties having rights determined by the interim orders had just had their "day in court" and a final determination of those issues.

5475

II. SPECIFICATION OF ERRORS IN THE COMMISSION ORDER ISSUED AUGUST 9, 1960

Underlying the above-stated grounds upon which Petitioners rely, it is submitted that the Commission's order issued August 9, 1960, included the following specific errors:

1. The Commission erred in its formal finding (2) that "The proposed increased rates filed in this proceeding

(5475)

by Tennessee, . . . are excessive and should be disallowed."

with particular respect to rates in Zones 1, 5 and 6.

2. The Commission erred in its formal finding (3) that "Tennessee should be permitted to file herein substitute lower rates satisfactory to the Commission . . . for the purpose of this interim order, . . . subject to refund in accordance with the Commission's order of April 29, 1960, and the undertaking heretofore filed by Tennessee in accordance with the terms of that order,"

with particular reference to rates in Zones 1, 5 and 6.

3. The Commission erred in its formal finding (4) that "Tennessee should be required to make prompt refunds with interest at 7 percent, in accordance with the Commission's order of April 29, 1960, and the undertaking heretofore filed by Tennessee, of all amounts collected by it from its jurisdictional customers subject to refund under its proposed increased rates. . . ."

with particular reference to rates in Zones 1, 5 and 6.

4. The Commission erred in its ordering paragraphs (A), (B), (C) and (D) with particular reference to refunds, filings and rates for the future in Zones 1, 5 and 6.

5476

5. The Commission erred in its ordering paragraph (G) and in its statements on pages 8 and 9 of the narrative recital of the order to the effect that the order is without prejudice to Petitioners and that Petitioners (and those similarly situate in Zones 2, 3 and 4) will be in the same position as they would have been under hypothetical conditions which are contrary to fact. To the contrary, Peti-

tioners are prejudiced by the interim reduction of rates in Zones 1, 5 and 6. Moreover, Tennessee filed its initial rates on the basis of a 7 per cent rate of return, and not a 6 1/8 per cent rate of return so that the Commission's hypothesis is contrary to fact, and as a result of said filing in Zones 1, 5 and 6 Petitioners derived an advantage under Section 4(e) of the Natural Gas Act as to their long-standing charge of undue rate preferences to certain of Tennessee's Zones.

6. The Commission erred in its statements on pages 7 and 8 to the effect that the propriety and legality of ordering Tennessee to make immediate refunds to customers in Zones 1, 5 and 6 had been settled in its recent *Southern Natural, supra*, order issued July 8, 1960.

7. The Commission erred in establishing a precedent herein which is contrary to the Natural Gas Act, the Administrative Procedure Act, and Constitutional guarantees of due process of law.

Respectfully submitted,

BROOKS E. SMITH

Brooks E. Smith

Attorney for

The Manufacturers Light and
Heat Company

The Ohio Fuel Gas Company

United Fuel Gas Company

Of Counsel:

BROOKS E. SMITH
JAMES G. O'NEILL

120 East 41st Street
New York 17, New York

Attorneys for

The Manufacturers Light and Heat Company
The Ohio Fuel Gas Company
United Fuel Gas Company

WILLIAM ANDERSON

JOHN P. EGAN, JR.

800 Union Trust Building
Pittsburgh 19, Pennsylvania

Attorneys for

The Manufacturers Light and Heat Company

W. F. LAIRD

RALPH N. MAHAFFEY

99 North Front Street
Columbus 15, Ohio

Attorneys for

The Ohio Fuel Gas Company

R. K. TALBOTT

HERBERT W. BRYAN

Post Office Box 1273
Charleston 25, West Virginia

Attorneys for

United Fuel Gas Company

Dated: August 29, 1960

5491

(Docketed Sept. 27, 1960)

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSIONBefore Commissioners: Jerome K. Kuykendall, Chairman;
Frederick Stueck, Arthur Kline and Paul A. Sweeney.

Docket No. G-19983

TENNESSEE GAS TRANSMISSION COMPANY

Order Denying Applications For Rehearing

(Issued September 27, 1960)

Applications for rehearing of the Commission's interim rate order issued August 9, 1960, in the above proceeding, have been filed by Tennessee Gas Transmission Company (Tennessee) and jointly by Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company (Intervenors).

Tennessee's application is directed to the allowance on common equity which the Commission found to be proper in determining the fair, just and reasonable rate of return to Tennessee for the purpose of the interim order, and to the interim rate reduction and refund provisions of the interim order. Intervenors' application is directed only to the interim rate reduction and refund provisions of that order.

Tennessee's proposed increased rates in this proceeding are based on a proposed overall rate of return of 7 percent. When filed, the proposed 7 percent rate of return was based on an allowance for common equity of 14 to 15 percent, which Tennessee contends has been the historical return on its book equity under Commission regulation. In February of 1960, subsequent to its filing in this proceeding,

(5491)

Tennessee issued additional common stock which had the effect of increasing the percentage of common equity in Tennessee's capitalization, and reducing the allowance on common equity produced by the proposed 7 percent rate of return to about 12½ percent, as computed by Tennessee. Tennessee did not thereafter propose any increase in its allowance on common equity, standing on the 12½ percent, as equivalent to its historical return on the basis of this thicker equity.

In our interim order of August 9, 1960, we found an allowance of between 10 and 10.5 percent on common equity to be fully adequate for Tennessee, and sufficient to enable it to attract new equity capital and preserve its financial integrity. We thereupon fixed a fair, just and reasonable overall rate of return of 6½ percent which, on the basis of the cost of debt and preferred stock and the capitalization ratios therein found to be proper for the purpose of the interim order, will produce for Tennessee an allowance on its common equity of 10.12 percent. Tennessee, in its application for rehearing, charges that our action in this respect was arbitrary and capricious, deprives it of property without due process of law, and discriminates against it in favor of other

5492

pipeline companies for which we have recently fixed rates of return. Tennessee cites our recent action in *Manufacturers Light and Heat Company*, 23 F.P.C. 446, February 25, 1960, and *Southern Natural Gas Company*, Docket No. G-20509, July 8, 1960, where, it contends, we allowed returns on common equity higher than that allowed Tennessee, and where the common equity was thicker than the common equity of Tennessee.

Tennessee states that in the *Manufacturers* case we allowed a return on common equity of 10.35 percent on an

equity ratio of 40.3 percent. On the contrary, we there found that a 6 $\frac{1}{4}$ percent rate of return was adequate for the period ending April 8, 1959, and that on the basis of a capital structure as of April 30, 1959, consisting of 59.7 percent debt and 40.3 percent common equity, and a cost of debt of 3.91 percent, an overall rate of return of 6 $\frac{1}{4}$ percent produced a 9.73 percent return on equity. We found that "a fair return on equity . . . should continue to approach 10 percent" and that since a 6 $\frac{1}{4}$ percent rate of return would not continue to produce a return on equity approaching 10 percent, because of the sharply increased cost of debt during 1959, a 6 $\frac{1}{2}$ percent rate of return which would produce a return on equity of around 10 percent should be allowed for the rates after April 8, 1959.

In the *Southern* case, as Tennessee states, we allowed a return on common equity of 10.18 percent. And as Tennessee also states, Southern's capital structure there consisted of 64.2 percent debt and 35.8 percent common equity. However, there is nothing inconsistent in our action in that case and in the present case. A lower equity ratio does not necessarily demand a higher rate of return as Tennessee contends. It may well be true that a high leverage condition with a thin equity is indicative of a greater risk than a low leverage, thick equity situation. But the equity ratio is only one element or factor to be considered in appraising the risks associated with the common equity of any given company, and certainly no mathematical measure of differences in risk can be derived from comparing the equity ratios of different pipeline companies. The total capital structure, including debt and preferred stock ratios as well as common equity, the stability of earnings, and the historical pattern of growth of a company are all factors to be considered in appraising risk and determining a proper allowance for common equity. Neither Manufacturers nor Southern has preferred stock

(5492)

in its capital structure, and neither has had the history of growth which Tennessee has had.

In our order of August 9, 1960, in this proceeding, as well as in other recent orders, we have stressed the variety of factors which must be considered in determining the allowance for common equity. Our finding that an allowance on Tennessee's common equity of between 10 and 10.5 percent is adequate and proper is not based solely upon the evidence of earnings-price ratios, nor have we assumed, as Tennessee would believe, that such ratios are a direct measure of a fair and reasonable return on the book value of the common equity. Such ratios are, however, an indication of the investor's appraisal of the risks inherent in an enterprise and the return he requires in the light thereof. as we have stated before, such ratios may properly be used with judgment, together with other factors, in determining a reasonable allowance on common equity.

5493

One such other factor is earnings on book equity, and Tennessee relies heavily in support of a higher allowance for equity on evidence of such earnings. We have given due consideration to this evidence as a factor in our determination of the allowance to be made, although such return cannot be taken as a direct measure of the allowance for equity. Such return includes contingent earnings under rates subject to refund in proceedings before the Commission. To fix a rate of return for the future on the basis of the historical return on book equity as Tennessee urges would be improperly to validate such contingent earnings.

The determination of a proper allowance for common equity is peculiarly a matter of judgment for the Commission. A rate of return cannot be a matter of slide rule computation. Consideration must be given to a multiplicity of factors, some of which cannot be isolated and objec-

tively measured and weighed, yet which, in the circumstances of any given case, may tip the balance one way or the other. In the present proceeding, we have considered all the evidence in arriving at our judgment of a fair and adequate allowance for Tennessee's common equity, and nothing in Tennessee's application for rehearing persuades us that our determination is incorrect or an improper exercise of administrative judgment.

In so affirming our interim order, we have also given consideration to, and we can find no sound basis for, Tennessee's charge that this determination will require Tennessee's stockholders to absorb virtually all of the increase in the cost of long-term debt incurred by Tennessee in the last five years. Tennessee has been able to maintain earnings on book equity at a fairly constant level during these years, and it appears that the increase in the cost of debt has been largely, if not completely, offset by Tennessee's ability to sell its common stock at prices well in excess of the book value of its stock. The record shows that Tennessee's common stock has been selling at about two and one-half times its book value. This further belies Tennessee's contention that our order will discourage its stockholders from expanding capacity, since the effect of raising new equity capital at prices in excess of book value is to increase the book value of its common stock. The rate of return as determined by our interim order will not adversely affect Tennessee's financial integrity, nor impair its continued growth. It is sufficient to attract new capital to Tennessee and provides a fair return to Tennessee on its net investment rate base.

Tennessee objects to any interim reduction of its rate of return with respect to its production properties. Tennessee, however, has not sought and the record shows no need for, a different rate of return on its production properties than on its pipeline properties. Accordingly, the 6 1/2 per-

(5493)

cent rate of return found to be fair, just and reasonable for the interim order applies to all of Tennessee's properties. It is true that this rate of return is subject to adjustment in the next phase of the proceeding, insofar as the production properties are concerned, by reason of the reservation of the question of how to treat tax benefits

5494

for statutory depletion and intangible well drilling costs in the light of *El Paso Natural Gas Company*, 22 F.P.C. 260 (1959) and *United Fuel Gas Company*, 23 F.P.C. 127 (1960). However, Tennessee will not be deprived during the interim period of any return to which it may be entitled by reason of such benefits, regardless of how the Commission finally disposes of this question—whether by an increased return on production properties or otherwise. Tennessee has included all such tax benefits to its cost of service and will be able to recover all such costs subject to refund pending the Commission's determination of the proper treatment of such benefits.

The interim order requiring refunds and providing for the filing of lower rates based on the $6\frac{1}{8}$ percent rate of return will result in annual savings to Tennessee's jurisdictional customers of \$11,001,825 pending final determination of Tennessee's rates in this proceeding, and is both necessary and appropriate to protect the interests of such customers. The order in no way prejudices the rights of any property in this proceeding, and, as we have found is a lawful exercise of our authority in carrying out the purposes of the Natural Gas Act.

The Commission finds:

The assignments of error and grounds for rehearing contained in the applications for rehearing of the Commission's order of August 9, 1960, in this proceeding, set

(5551)

forth no new facts or principles of law which were not fully considered by the Commission when it issued that order, or which having now been considered warrant any change or modification thereof.

The Commission orders:

The above applications for rehearing of the Commission's order of August 9, 1960, in this proceeding, are hereby denied.

By the Commission. Chairman Kuykendall dissenting.

J. H. GUTRIDE

Joseph H. Gutride,

Secretary

5551

(Received June 13, 1960)

UNITED STATES OF AMERICA
BEFORE THE FEDERAL POWER COMMISSION

Docket No. G-19983

In the Matter of

TENNESSEE GAS TRANSMISSION COMPANY

**Memorandum of Tennessee Gas Transmission Company in
Opposition To Staff Motion for Interim Order**

On May 25, 1960, after the completion of the evidence on the issue of rate of return, Staff Counsel orally moved that the Commission issue an interim order determining the issue of rate of return. The motion contemplates that if the Commission finds that a rate of return of less than 7% (the return claimed by Tennessee in this case) is fair and reasonable, immediate refunds and rate reductions by Tennessee would be ordered to the extent that the revenues from the filed rates exceed the resulting lower cost of service. For the purpose of the interim order only,

(5551)

Tennessee's presentation as to rate base, method of allocation, and cost of service (other than rate of return and related income taxes) is to be used. Omission of the intermediate decision procedure was also requested as to the issue of rate of return (Tr. 1616-1617).

For the reasons discussed below, Tennessee opposes the Staff motion

I

At the outset we wish to make it crystal clear that Tennessee wholeheartedly supports the Commission's efforts to expedite the trial and decision of rate cases. We also wish to make it clear that while we doubt that the piecemeal trial and disposition of certain selected issues will,

5552

in itself, result in the over-all expedition of rate cases, we would, nevertheless, in the spirit of cooperation not oppose an interim order on the issue of rate of return, if that issue were independent of other issues. However, we must, and do, vigorously oppose the interim order procedure in this particular case due to the fact that an inseparably related issue—the issue of zone allocation—is, as yet, undecided. We respectfully submit that, because of this fact, an interim order requiring refunds and rate reductions would be unlawful.

II

As the Commission knows, prior to Docket G-5259, every Tennessee rate case was disposed of by agreement among the Commission Staff, Tennessee and Tennessee's customers. Those agreements went to the over-all cost of service as well as to the rate differentials among the zones on the Tennessee system. The issue as to the method to be used for allocating costs among Tennessee's six rate zones was raised in Docket G-5259, but, with the consent of

all concerned, was dismissed in view of the fact that the issue was involved in the then (and still) pending rate case in Docket G-11980.

After Tennessee completed the presentation of its direct case in Docket G-11980, a motion was filed on March 17, 1959, by the Consolidated system companies requesting that the zone allocation issue be severed from the cost of service issue, and that the case proceed to hearing and decision first on the zone allocation issue only. This motion was granted by the Commission's order of April 30, 1959. Lengthy hearings have been held and extensive briefs have been filed. The matter is now pending a

5553

decision by Presiding Examiner Zwerdling.

The method of allocation advocated by Tennessee is a combination of the two principal methods previously followed by the Commission in assigning costs to zones, namely, (1) the Mcf-mile method of allocation, and (2) the application of historical rate differentials. The Staff and New England intervenors advocated the Mcf-mile method (with certain differences not pertinent here). The Consolidated system companies and the Columbia system companies advocated variations of the zone by zone (zone gate) method of allocating costs.

No new cost allocation evidence has been presented in the instant docket. The Examiner has ruled that in view of the pendency of that issue for decision in Docket G-11980, he will not re-try that issue in the instant case (Tr. 302). Tennessee agrees with this ruling.

III

The fact that different methods of allocation have been proposed is not important in and of itself. What is im-

(5553)

portant however—and of crucial significance so far as the Staff's motion is concerned—is the fact that the respective zones as well as services (and, indeed, even the demand and commodity components); are allocated a different proportion of Tennessee's over-all cost of service *depending upon which method of allocation is used to allocate that cost of service*. For example, reference to Exhibit 139 (pp. 1-5) in Docket G-11980 shows the following differences in costs allocated to gas sales in the six Tennessee rate zones by the

5554

different methods of cost allocation (and variations thereof) proposed in that proceeding.²

Sales-Zone	Tabulation A				
	(1) Columbia	(2) Consolidated	(3) New England	(4) Staff	(5) Tennessee
Southern	\$ 23,014,151	\$ 22,131,880	\$ 23,182,434	\$ 23,142,175	\$ 22,683,241
Central	17,067,755	16,891,574	17,533,137	17,361,176	17,461,793
Eastern	62,037,218	62,233,762	67,976,129	67,029,625	66,460,794
Northern	32,534,546	32,963,603	33,572,626	32,530,478	33,603,195
New York	26,613,333	27,937,077	26,394,342	26,367,457	27,014,352
New England	23,852,427	21,607,221	16,823,086	19,354,014	18,614,416
Total ³	\$185,119,430	\$184,765,117	\$185,481,754	\$185,784,925	\$185,737,791

It can be readily seen from the above tabulation that differences of as much as approximately \$7,000,000 a year in the costs allocated to a particular zone can result on the

¹ We have utilized, without prejudice, the Staff's claimed cost of service in Docket G-11980 for the purpose of this illustration.

² While the figures in Tabulation A would in all cases be different in the instant proceeding inasmuch as we are dealing with a different cost of service, the Docket G-11980 figures are, nevertheless, valid for the purpose of illustration.

³ The relatively minor differences in the various totals are due to the differences in the balance of the cost of service allocated to Transportation and non-jurisdictional services. Those differences are reflected in Exhibit 139 in Docket G-11980, but are not pertinent to this comparison.

(5555)

Tennessee system from the use of different allocation methods. Thus, Columbia would allocate \$23,852,427 a year to the New England zone under its zone gate method of allocation, whereas the New England intervenors would allocate \$16,823,086 to that zone under the Mcf-mile method. Columbia would allocate to the Eastern zone \$62,037,218 whereas the New England intervenors would allocate \$67,976,129 to that zone. Under the method proposed by Tennessee, \$18,614,416 would be allocated to the New England zone and \$66,460,794 would be allocated to the

5555

Eastern zone.

It can also readily be seen from the foregoing that unless the rates filed by Tennessee in each zone produce revenues equal to the cost of service allocated to each zone under the allocation method ultimately selected, a retroactive rigid application of the selected method of allocation would prevent Tennessee from recovering its total cost of service. This is so inasmuch as the excess revenues in certain zones later found to be refundable, could not then be offset by a retroactive increase in other zones' revenues.

IV

As previously stated, the Staff's motion contemplates that such refunds and concomitant interim rate reductions as may be required by an interim order will be made on the basis of the Tennessee method of cost allocation and rate design. Such procedure has surface plausibility. Closer analysis, however, indicates conclusively that the procedure cannot legally, and should not as a practical and equitable matter, be adopted in this particular case.

Under the Natural Gas Act, Tennessee files *rates* (not cost allocations) for each zone. Before such filed *rates* for any particular zone can be reduced by way of an interim

(5555)

order or by way of a final order at the conclusion of the proceeding, there must be a finding that the rates for the zone in question are unjustly or unreasonably high. But *how can the Commission make such a finding without first having determined the method of cost allocation to be employed to test the reasonableness of those rates?* Where the method of cost allocation has been determined or is not in issue,

5556

the Commission is not confronted with such a problem. But where, as here, the method to be employed in allocating costs among zones on the Tennessee system is pending decision, we submit that the required finding cannot be made until the allocation issue is determined.

Moreover, one of the very matters at issue in Docket G-11980 is whether the Commission, if it adopts a method of cost allocation different from Tennessee's, should make its method retroactive to July 14, 1957 (the date the G-11980 rates became effective subject to refund), or whether such different method be made prospective only from the effective date of the allocation order. Tennessee has taken the position that any new method of allocation adopted by the Commission should be made prospective only; that it would be wholly inequitable and a denial of due process to apply a new allocation method retroactively, if such application deprived Tennessee of any part of the rate of return to which it is entitled. The Columbia companies and the New England intervenors contend that, as a matter of law, any new method of allocation must be applied retroactively to the beginning of the refund period. The Staff contends that any new method of allocation be applied retroactively, but qualifies its position by observing that the serious impact on Tennessee that might result by reason of a retroactive application of a method different from that used by Tennessee must "be given weighty con-

sideration, which, in part, would at the appropriate time reflect the judgment of the Presiding Examiner or the Commission whether the method approved should be rigidly applied to the past period" (Staff Brief in Docket G-11980, p. 58).

As previously stated, the instant motion of the Staff contemplates

5557

that the Tennessee allocation method would be used to make interim refunds and rate reductions stemming from the proposed interim rate order on rate of return. However, if, subsequent to making such interim refunds and rate reductions, a method of allocation different from that used in making the interim refunds and rate reductions is applied retroactively to the beginning of the refund period, Tennessee would, as stated above, be unable to recover its total cost of service, inasmuch as Tennessee cannot file a retroactive increase in rates. In other words, the Commission cannot lawfully now determine the rate of return to which Tennessee is entitled, when a later *nunc pro tunc* determination on a related phase of the case (allocation) could prevent Tennessee from earning the full rate of return allowed.

Thus, suppose, for illustrative purposes, that the total cost of service assigned to the sales zones in an interim order is \$185,784,925 (which is the Staff proposed jurisdictional cost of service for the sales zones in Docket G-11980 shown in the above tabulation). If Tennessee's method of cost allocation is used, interim refunds and rate reductions would be predicated on the allocation of costs to the six Tennessee rate zones shown in column (5) of Tabulation A above. Should, however, either the Columbia method or the New England method of cost allocation be subsequently adopted and applied retroactively, the

(5557)

following excesses or deficiencies in revenues would result in the several rate zones:

5558

*Excess or (deficiency) of Revenue Resulting
from Subsequent Cost Allocation Determination*

Zone	Columbia Method ⁴	New England Method ⁵
Southern	\$ (330,910)	\$ (499,193)
Central	394,038	(71,344)
Eastern	4,423,576	(1,515,335)
Northern	968,649	(69,431)
New York	401,019	620,010
New England	(5,238,011)	1,791,330

It can readily be seen from the first column of figures that Tennessee, under the circumstances assumed, would, when the final allocation order is entered, have to make *additional* annual refunds of \$5,687,282 in all zones except the Southern and New England zones. Of vital importance, however, is the fact that in the latter two zones, Tennessee would have previously refunded, pursuant to an *interim order*, a total of \$5,568,921 per year too much (or collected insufficient revenues by such amount) which it could not recoup. It would, therefore, have been deprived of the right to earn the allowed rate of return by the same amount.

From the second column of figures, it can be seen that, under the same circumstances assumed, Tennessee would, when the final allocation order is entered, have to make an *additional* refund in the New York and New England zones, but as to the remaining four zones it would, pursuant to an *interim order*, have previously refunded \$2,145,303 per year too much (or collected insufficient revenues by such

⁴ Differences between columns (1) and (5) of Tabulation A.

⁵ Differences between columns (3) and (5) of Tabulation A.

amount), thereby preventing it from earning the allowed rate of return by the same amount.

5559

Patently, the situation depicted above would result in confiscation because Tennessee would be deprived of the earnings available from the rate of return to which it is entitled.

V

It may be contended that the situation described above could only come about if the Commission were to require the selected method of allocation to be applied retroactively; but that the Commission, if it issues an order requiring interim refunds and rate reductions, would not thereafter put the company in a position where it would be denied the right to recover the allowed cost of service. If such contention is made, it would appear to presuppose that the Commission will not make any new method of allocation retroactive. While we are of the view that any new method of allocation adopted for the Tennessee system should, and legally can, be made prospective only, others, as shown above, are of a different view. If they should ultimately prevail before the Commission or the Courts, Tennessee, regardless of the equitable intentions of the Commission, would suffer irreparable financial loss from having made interim refunds and rate reductions prior to a final decision on zone cost allocation.

Apart from the foregoing, it would seem to us that such contention, if made, presupposes a pre-judgment by the Commission of the very issue now pending before Examiner Zwerdling in Docket G-11980. As stated above, the question of prospective or retroactive application (or degree of retroactive application) of the method of allocation to be selected is pending decision in Docket G-11980. It seems to us that basic fairness to Tennessee and all of

(5559)

its customers requires that such issue not be prejudged—as it were—by the Commission taking action now by way of an interim rate order which will make it more difficult for the Commission later to decide the issue unfettered by the consequences flowing from a hasty previous action.

5560

VI

It is no answer to say—as may be contended by the Staff—that Tennessee has the responsibility of filing rates; that it must assume the risk that those rates will not recover the cost of service in the event such rates were designed on the basis of a method of allocation different from that which the Commission ultimately selects, as the fairest method for the Tennessee system; and that, therefore, it is appropriate to place the responsibility on Tennessee for selecting the method to be used for allocating costs to zones for the purpose of making interim refunds and rate reductions. Assuming, *arguendo*, that when Tennessee filed increased rates it assumed the type of risk discussed above, such risk is one voluntarily assumed by Tennessee. A risk voluntarily assumed is one thing. It is quite another thing when the Commission, by order, imposes and increases the risk upon Tennessee of not being able to recover the rate of return allowed by the Commission. And, as shown above, such a risk would be imposed upon Tennessee if interim refunds and rate reductions are ordered, without first having determined the method of cost allocation and rate design to be used. The imposition of such a risk, we submit, would be unlawful.

Moreover, from the standpoint of simple fairness—assuming *arguendo* the legal validity of an interim refund and rate reduction order in this case—Tennessee should not be put in the position of not being able to earn the return to which it is found to be legally entitled because

of its inability to predict the allocation method ultimately to be adopted. Tennessee has selected a method of allocation which, in its judgment, is fair to all the customers on its system. The method selected,

5561

as stated above, combines the two methods previously used by the Commission in allocating costs on pipeline systems. But, as pointed out in our Initial Brief (pp. 3-6) in Docket G-11980, cost allocation "is not a matter for the slide rule." On the contrary, "it involves judgment on a myriad of facts. It has no claim to an exact science." In other words, "consideration of fairness, not mere mathematics, govern the allocation of costs." *Colorado Interstate Gas Co. v. Federal Power Commission*, 324 U.S. 581, 589, 591 (1945). Should the Commission now embrace a method of cost allocation different from those previously prescribed or approved by it, considerations of fairness, we respectfully submit, dictate that Tennessee should not be penalized by a *nunc pro tunc* order applying such new and different method. And if this be so, certainly simple logic and fairness also dictate that no interim order be adopted which can put Tennessee in such jeopardy. This is particularly so because no customer can be prejudiced by a denial of the instant Staff motion, in view of Tennessee's obligation to refund excess charges with interest.

VII

Tennessee is greatly interested in expediting the disposition of its rate cases. It desires to, and will, cooperate with the Staff and the Commission to that end. It feels most strongly and keenly, however, that because of the pendency of the allocation issue, an interim order is clearly unlawful and, if issued, would unduly complicate this case.

We urge the Commission, therefore, in view of all the circumstances and considerations discussed above, to deny

(5561)

the Staff's motion. This is especially appropriate in view of the fact that the zone allocation issue

5562

is now pending decision by Examiner Zwerdling, and a decision thereon by the Examiner and the Commission can be expected in the reasonably near future. Indeed, we are inclined to the view that the ultimate disposition of the three pending Tennessee rate cases will be hastened by the early disposition of the cost allocation issue.

VIII

We have been able to find three cases where interim rate orders of the Commission have been sustained by the courts, namely, *F.P.C. v. Natural Gas Pipeline Company of America*, 315 U.S. 575 (1942); *State Corporation Commission of Kansas v. F.P.C.*, 206 F. 2d 690 (8th Cir., 1953); and *Panhandle Eastern Pipe Line Co. v. F.P.C.*, 236 F. 2d 606 (3rd Cir., 1956). None of those cases we submit constitute legal precedent for the type of interim order proposed by the Staff here.

The *Natural Gas Pipeline* case was a Section 5(a) proceeding, wherein for the purpose of issuing an interim rate reduction order, the Commission accepted the company's claimed cost of service, except for the element of rate of return which was decided upon the basis of a complete record. It must be noted, however, that the Commission's order was *prospective* only. There was no possibility that a later order in the same case could be made *retroactive*. Thus, there was no possibility that *Natural Gas Pipeline* could be deprived of any part of its cost of service by a later order in the same case. This case, therefore, clearly is no precedent for the Staff's motion.

The *Kansas Corporation* case (*Northern* case) involved a situation wherein three separate rate increases had been filed by *Northern*. While

5563

the third increase (Docket No. G-1881) was still in the hearing stage, the Commission decided the first two cases (Opinions 228 and 228-A; 11 F.P.C. 123). Opinions 228 and 228-A effectively disposed of various issues upon which \$7,601,853 of Northern's third rate increase was predicated. As noted by the court (206 F. 2d at p. 715), items of increase aggregating \$7,601,853 "in the third rate increase proposal were items included in and tried out and decided adversely to Northern by the Commission in Opinion No. 228." In view of that fact, the Commission granted a motion dismissing Northern's third rate increase to the extent that the issues involved had just been decided adversely to Northern's contentions. Northern obtained a stay pending review of all three orders.

Unlike the instant case, there was no outstanding zone allocation issue. On the contrary, at that time Northern had uniform system-wide rates. Thus, there was no possibility that a subsequent order in the same docket (G-1881) could operate retroactively to prevent Northern from recovering its full cost of service. While further rate reductions were possible in Docket G-1881, no such reductions were possible with respect to the issues finally decided in Opinions 228 and 228-A. In other words, no subsequent order could injure Northern in the manner herein discussed.

The *Panhandle* case is practically identical to the *Northern* case. That part of Panhandle's rate increase in Docket G-2506 which was predicated upon issues just decided in Opinion 269 was dismissed, since no change in circumstances had (according to the Commission and Court) been shown. Here also, no allocation of costs to zones remained to be decided. Indeed, one of the issues dismissed was the issue of allocation of cost of service inasmuch as that issue had been decided in Opinion 269.

(5564)

5564

shortly prior to the filing in Docket G-2506. As in the *Northern* case, any subsequent opinion in Docket G-2506 could not operate retroactively to deprive Panhandle of the ultimate cost of service allowed by the Commission in that docket.

We come now to an order issued on April 29, 1960 in the current *Panhandle* rate case in Docket G-19780. In that case, as the Commission knows, it set for hearing in the first phase of the case, certain issues, including rate of return. The Commission specifically noted in its order that among the issues to be disposed of in the first phase of the case would be "a cost of service utilizing the allocation principles relied upon by the Commission in Opinion 269, as modified in *City of Detroit v. F.P.C.*, 230 F. 2d 810." The matter of cost allocation was not involved, however, in the *City of Detroit* case, unless the Commission, by the quoted language, meant the allocation of costs to the gasoline extraction operations. Be that as it may, the fact is that, in the current *Panhandle* rate case, confusion has arisen as to whether or not cost allocation and rate design principles are at issue in the first phase of the case. Counsel for Panhandle interprets the order as meaning that cost allocation and rate design are at issue. Staff Counsel contends that those matters are not in issue. The Presiding Examiner in that case has permitted evidence pertaining to cost allocation and rate design to be introduced in the first phase of the proceeding. On June 8, 1960, Staff Counsel stated that he would take an appeal to the Commission from the ruling of the Examiner permitting such evidence to be introduced.

5565

It is not our purpose to argue the pros and cons of the recent Panhandle order. We think it is important to point

(5566)

out, however, that in Opinion 239 the Commission adopted a method of cost allocation for the Panhandle system. No method of cost allocation has ever been adopted by the Commission for use on the Tennessee system. That there is a need for an early decision as to the method of cost allocation to be used on the Tennessee system is attested to by the Commission's aforementioned order of April 30, 1959 (in Docket G-11980) requiring the hearing and decision on the cost allocation issue to precede the hearing and decision on the cost of service issues in that docket. That hearing has been completed. Briefs have been filed. A decision will soon be forthcoming. These facts are not present in the Panhandle case. These facts, we submit, clearly require a denial of the Staff's motion herein, wholly aside from the propriety or impropriety of the Commission's action in the Panhandle case, as to which Tennessee takes no position here.

IX

In addition to the arguments and reasons set forth above in opposition to the interim order procedure, there is a special circumstance which provides a peculiarly cogent reason for not issuing an interim order in this case. It is the imminence of a decision on the cost allocation issue now pending in Docket G-11980.

The zone cost allocation issue in that docket has been tried in great detail and at great expense over a long period of time. A decision by the Presiding Examiner should be forthcoming in the near future. As noted previously, the Examiner in the instant case (who is also the Examiner

5566

in Docket G-11980) has properly ruled that the allocation issue is not to be retried in this case. In other words, the allocation method selected in Docket G-11980 will be applicable to the instant case.

(5566)

In the light of the foregoing, apart from the legal questions involved, it would be imprudent and impractical, as well as expensive, if Tennessee were required to make new rate filings as a result of an interim order, and shortly thereafter be faced with the necessity of substituting a different set of rates as a result of the decision on the allocation issue. We respectfully submit that sound administration and logic requires waiting the relatively short time involved until the decision on the allocation issue is made.

In the light of all of the foregoing, we urge the Commission to deny the Staff motion.

REQUEST FOR ORAL ARGUMENT

In view of the importance of this matter, we respectfully request the opportunity to argue the matter orally before the Commission.

Respectfully submitted,

TENNESSEE GAS TRANSMISSION COMPANY

By /s/ HARRY S. LITTMAN

Harry S. Littman

Its Attorney

W. C. BRADEN, JR.

B. J. WILLIAMSON

Tennessee Building

Houston 1, Texas

HARRY S. LITTMAN

JACK WERNER

HAROLD L. TALISMAN

317 Wyatt Building

Washington 5, D. C.

Attorneys for Tennessee Gas Transmission Company

June 13, 1960.

5577

(Received June 13, 1960)

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Docket No. G-19983

In the Matter of

TENNESSEE GAS TRANSMISSION COMPANY

Memorandum. Answer and Objections of the Manufacturers Light and Heat Company, the Ohio Fuel Gas Company and United Fuel Gas Company to the Motion of Staff Counsel For Interim Refund Order.

The Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company (Columbia Companies), Intervenor herein, pursuant to the direction of the Presiding Examiner (T. 1629), respectfully state that:

(1) A prompt decision on the rate of return issue in this proceeding, together with a prompt decision by the Presiding Examiner of the allocation issue now pending in Docket No. G-11980, would open the door to settlements of Tennessee's three pending rate cases.

(2) Columbia Companies would agree to a waiver of the intermediate decision procedure for the limited purpose of determining a proper rate of return for Tennessee in this proceeding.

(3) Columbia Companies must oppose the Staff proposal for an interim refund order because such an order (a) would aggravate and complicate a long-standing and serious situation of undue discrimination in Tennessee's rates, and (b) would be illegal in view of the status of the allocation issue.

In respect whereof Columbia Companies state:

I. THE CONTROVERSY IN CONTEXT

The broad problem involved pertains to a determination

5578

of just and reasonable rates for Tennessee Gas Transmission Company (Tennessee) from and after April 5, 1960, at which time the filed rates became effective subject to refund. The Staff motion seeks interim, or tentative changes in Tennessee's effective rates. These tentative rates would then be subject to a subsequent determination that the same are too high or too low with respect to any particular rate schedule and zone. In short, the Staff would have quick action ordering piecemeal refunds to particular customers* before the completion of final determinations in prior dockets and before full hearings in this docket. Contrasted with this is the approach of Columbia Companies who seek a speedy final determination of the just and reasonableness of Tennessee's rates within the confines of the legal procedures set by the Natural Gas Act and Administrative Procedure Act.**

A. The Status of Pertinent Proceedings

This proceeding, Docket No. G-19983, is the third of three pending rate cases of Tennessee. The underlying rates of Tennessee were determined after a settlement in Docket

* At T. 1624, Staff Counsel opines that the "small customers" of Tennessee are interested in quick refunds "in order to be able to sell the gas that they are purchasing from Tennessee," and leaves the inference that such are entitled to preference over the interests of the "larger intervenors" which may result from the cost allocation determination. There is no warrant in the record for these gratuitous and debatable assumptions or opinions.

** "Motion To Expedite Proceedings" dated May 14, 1960, filed by Columbia Companies in Docket Nos. G-11980, G-17166 and G-19983.

(5580)

No. G-5259, by order issued October 17, 1957. The two pending

5579

rate cases; Docket Nos. G-11980 and G-17166, which were initiated prior to the instant case, have the following procedural status:

Docket No. G-11980. Tennessee's rates filed in this docket became effective subject to refund on July 14, 1957. These rates were in effect for twenty-two months until they were superseded by the rates in Docket No. G-17166 on May 15, 1959. Hearings commenced in Docket No. G-11980 on April 16, 1957, and continued intermittently until December 17, 1959. *On the separated issue of cost allocation,* the hearing has been closed. Initial and Reply Briefs were filed on March 14 and April 11, 1960. The issues relating to the allocation of costs among Tennessee's various rate zones and classes of customers is now pending before the Presiding Examiner for an interim decision, which, when acted upon by the Commission, will have a controlling effect in subsequent Tennessee dockets. (Cf. G-19983, T. 299-302)

Docket No. G-17166. The Tennessee rates involved in this docket became effective on May 15, 1959, and were in effect for almost eleven months until superseded on April 5, 1960, by the rates filed in Docket No. G-19983. No hearings have been held with respect to G-17166, with the exception that the cost allocation determination in Docket No. G-11980 was specifically contemplated by the Commission to be

5580

applicable to this proceeding.*

* By its order covering issues in Docket No. G-11980 issued April 30, 1959, the Commission stated:

"Hearings in this proceeding were commenced on April 16, 1959, and have proceeded through cross examination on Tennessee's case in chief

(5580)

Docket No. G-19983. The instant proceeding, Docket No. G-19983, as aforesaid, pertains to Tennessee's rates which became effective subject to refund on April 5, 1960. Hearings commenced on February 2, 1960, and have been held intermittently for 13 days through May 25, 1960. Tennessee presented its direct case upon all of the issues involved, including the individual items of cost of service, cost allocation and proposed rates. Of these issues the "rate of return" element of Tennessee's total cost of service is the only one in relation to which the evidentiary record is closed. Tennessee's rate of return presentation was contested by several of the parties and rebuttal evidence on that single issue was presented. As to all issues, other than rate of return, none of the Tennessee witnesses have been cross-examined and none of the parties to the proceeding have been permitted to offer rebuttal evidence.

5581

The Examiner would *not* permit evidence showing the allocation of return among zones and services in any manner other than that proposed by Tennessee.* Tennessee used the same method which was so hotly contested in

and preparation and service of proposed testimony and exhibits by the Staff and intervenors. Reconvening of hearings herein is presently scheduled for May 12, 1959. In the interim Tennessee has proposed a further rate increase at Docket No. G-17166. The level of rates determined in this proceeding may thus be effective only for a 'locked-in-period.' *It is our view that separate and prior hearing on the issues relating to the principles and methods to be applied toward allocation of costs among the zones on Tennessee's system and among the classes of service within the zones will aid in the disposition of this proceeding and may be of similar aid in disposition of proceedings in Docket No. G-17166.*"

We endorse wholeheartedly the underlined statement of the Commission.

* In point of fact the Presiding Examiner has specifically ruled that he will not receive rebuttal evidence on the issue of cost allocation with or without a reduction in allowable return. (T. 302, 1235-1241)

Docket No. G-11980, which is now pending before the same Examiner.

The record would therefore only permit a determination of a part of the rate of return issue. If a determination should be made as to the amount of return to which Tennessee is entitled without a determination as to what portion of such return should be paid by Tennessee's various zones and classes of customers, Tennessee would not be able to make a refund of the excess. It would not know to whom and in what amounts any such refund should be made. Tennessee could not make refunds on the basis of its own proposed allocation method, knowing full well that such allocation method may not be approved by the Commission or the Courts.

The Commission cannot lawfully require refunds to be made in any particular manner without first permitting Tennessee and its customers to be heard with respect to the allocation of such refunds. Such action would either (a) predetermine issues not previously decided in any case, and not yet heard in this proceeding and with respect to which the parties have been denied the opportunity to offer evidence, or (b) subject Tennessee to a retroactive decision as to how it should have made the refunds. Such action would either deprive Tennessee's customers of due process of law by prejudging the

5582

the allocation issue or subject Tennessee to confiscation of its property if its proposed allocation method is rejected.

B. Staff Motion; Examiner's Direction

In this context Staff Counsel moved orally on the record: "that the record on rate of return be considered and an order issued thereon determining the fair rate of return for Tennessee."

(5582)

and

"depending upon the . . . fair rate of return that is determined, if it is anywhere lower than 7 percent, that immediate refunds be ordered by Tennessee for the difference between the claimed or the proposed 7 percent of return and that determined . . . and that for the purpose of that immediate refund all other presentation insofar as rate base and method of allocation between the zones be used as presented by Tennessee" (T. 1616).

In addition to either supporting or opposing the Staff motion, the Examiner directed the parties to give their views

"not only to the question of whether there should be an interim order or decision, but also as to what type of refund order should be issued as a result of the interim decision" (T. 1635).

II. COLUMBIA COMPANIES ARE OPPOSED TO ANY INTERIM REFUND ORDER IN THIS PROCEEDING

A. *An Interim Refund Order Would Aggravate and Complicate Tennessee's Unduly Discriminatory Rate Situation.*

For many years and in many proceedings Columbia Companies have been complaining to the Commission and the Courts that Tennessee has been *overcharging* them and those similarly situated in Tennessee's Zones 2, 3 and 4, and at the same time *undercharging* customers in Tennessee's Zones 1, 5 and 6. Columbia Companies' complaints remain unresolved to date. Columbia Companies contend that Tennessee has violated

Section 4(b) of the Natural Gas Act with respect to undue rate discrimination. Columbia Companies have contended that this rate discrimination is due in large part to Tennessee's method of cost allocation underlying its rates to certain classes of customers in its six rate zones.

This cost allocation controversy alone involves millions of dollars. For example, a determination of this single issue in Docket No. G-11980 could adjust Tennessee's costs and rates based thereon among its six zones, as follows:

Results of Cost of Service Studies By Zones

*Tennessee Method Compared with Columbia Method**

Zones (1)	Tennessee Study (2)	Columbia Companies Study (3)	Tennessee Study Compared To Colum 3 Efficiency (4)	Excess (5)
1 (Southern)	\$ 22,683,241	\$ 23,044,151	\$ 330,910	—
2 (Central)	17,461,793	17,067,755	—	\$ 394,038
3 (Eastern)	68,785,167	64,061,375	—	4,723,792
4 (Northern)	41,086,996	39,478,529	—	1,608,467
5 (New York)	31,349,226	32,414,825	5,238,011	—
6 (New England)	18,614,416	23,852,427	5,238,011	—
Total	\$199,980,839	\$199,889,062	\$6,634,520	\$6,726,297

It is clear that if Columbia prevails on the allocation issue in Docket No. G-11980, Tennessee will have allocated more than 61½ million dollars too much to the middle rate zones and that its allocations to other zones will have to be increased by more than 61½ million dollars. This comparison points up the fact that it is impossible for Tennessee to refund any excess revenues until the Commission decides

* These cost allocation comparisons are derived from Docket No. G-11980, Exhibit 128, line 7 (one of four studies made by Columbia Companies) and line 10 (Tennessee study); see Tab M, Appendix to Columbia Companies' Brief dated March 16, 1960.

(5583)

which of Tennessee's customers have been overcharged and in what amounts.

5584

It is impossible to determine a comparable range of similar cost allocation adjustments in Docket No. G-19983 because the Examiner's rulings aforesaid have precluded the other parties from determining or introducing evidence upon the cost allocation issue other than that used by Tennessee in its filing. However, it is clear that any such similar adjustment would be substantial.

Faced with such an important contested issue now ripe for determination in Docket No. G-11980, Columbia Companies must oppose any immediate piecemeal refund which is based upon Tennessee's method of cost allocation as a prejudicial aggravation of Tennessee's unduly discriminatory rates.

Historical increases in Tennessee's rates have been *disproportionately* higher in Tennessee's Central and Eastern Zones than in other zones, wherein Columbia Companies purchase substantial volumes of gas in each of the many settlements of Tennessee's cases *since 1947*.^{*} It is submitted that the application of Tennessee's method of cost allocation in an interim refund order would merely cause a progressive deterioration of the unjustifiable rate preferences shown of record in Docket No. G-11980.

B. An Interim Refund Order Herein Would Be Contrary to Statute and an Abuse of the Administrative Process.

As stated above Columbia Companies and others have been precluded by the Examiner from submitting evidence

^{*} See Columbia Companies' Answer to a recent Motion of Consolidated Natural Gas System in Docket No. G-11980, pages 6-7.

on the issue of the allocation of costs in this proceeding. On the other

5585

hand Tennessee and the Commission Staff have been permitted to adduce cost allocation evidence confined to the Tennessee method. It should be emphasized that the Tennessee method of cost allocation has been the subject of complaint by Columbia Companies and others at least from the trial of issues in Tennessee's Docket No. G-5259. *Therefore, there has never been any determination by the Commission on an evidentiary record of the proper method of cost allocation on the Tennessee system.*

Columbia Companies have been denied in advance their right to contest the cost allocation basis upon which the Staff would have the Commission issue an interim refund order. The law is plain that Columbia Companies have a right to adduce evidence on any important and unresolved material issue of facts involved. For example:

1. *Controlling Statute and Rule.*

Natural Gas Act, Section 1(e).—This Act provides "That . . . after full hearings, either completed before or after the rate, charge, classification or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective . . . where increased rates or charges are thus made effective, the Commission may . . . require . . . or bond . . . to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase . . . and upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such in-

(5586)

*creased rates or charge by its decision found not justified."**

The statute requires a "full hearing" prior to a refunding order. Columbia Companies have not had a full hearing.

5586

The hearing is not complete even upon the first of the piecemeal portions. The proceeding is not ripe for Commission order "upon completion of the hearing." Here the Commission could only order interim refunds on the basis of *expediency* and could not comply with the statutory requirements that the refunds of the portion of Tennessee's increased rates or charges were "found not justified." Justice demands fair treatment to all. Until the cost-allocation issue is determined, fair treatment to all is impossible by an interim refund order.

Administrative Procedure Act, Section 7(c)—This section of the Administrative Procedure Act precluded an order by a Commission

"except upon consideration of the whole record or such portions thereof as may be cited by any party and as supported by and in accordance with the reliable, probative, and substantial evidence. Every party shall have the right to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts."

Because of the Examiner's ruling preventing Columbia Companies from adducing evidence on cost allocation, it would be impossible for the Commission to comply with

* Emphasis supplied in quotations throughout this Memorandum.

this provision of the Administrative Procedure Act, since any order now must necessarily be based upon a truncated and incomplete evidentiary record.

Commission Rule 1.20 (g) (1). Order 217, issued November 20, 1959, in Docket No. R-177 reiterated the procedural truism that

5587

"parties and Staff Counsel shall have the right of presentation of evidence, cross-examination, objection, motion, argument and appeal."

Thus, it is clear that if Staff Counsel has been permitted to adduce evidence of cost allocation and the other parties have not been given equal opportunity, the ordinary principles of fair play have been patently violated.

In the background proceeding involving Tennessee's underlying rates, Docket No. G-5259, the Commission itself recognized the legal principles involved herein. In its Order Granting Motion In Part, issued September 20, 1956, at pages 5 and 6, the Commission stated:

"Since Tennessee is engaged in rendering jurisdictional and non-jurisdictional service, it is not possible to translate the 'total' of Tennessee's cost of service into jurisdictional 'rate level' without first determining the portion of the 'total' properly allocable to jurisdictional sales. Accordingly, even though we find that it is now appropriate to determine the 'total' of Tennessee's cost of service, such cost of service cannot be translated into jurisdictional rates (or 'rate level') until decision is made as to the proper method of allocating the 'total' between jurisdictional and non-jurisdictional sales."

"Moreover, our experience tells us that if in the future a change in Tennessee's zone boundaries or rate differentials is in order, the effect of the resultant rate on particular customers will differ dependent upon what cost of service is found proper here. *On this record, however, it is not possible to now determine what the effect upon particular customers will be until resolution of the cost of service and zone issues.*

"*Thus, we are of the opinion that it would not be only premature for us to grant that part of Tennessee's motion requesting that we at this time fix rates to be effective on and after December 15, 1954, it would also be unfair and improper.*"

5588

2. *The Cases Apparently to be Relied Upon by the Staff Are Not Precedents for the Order Sought.*

At T. 1625-1627 the Examiner referred to a recent Commission order issued April 29, 1960, *In the Matter of Panhandle Eastern Pipe Line Company*, Docket No. G-19780. Although the order specifically avoided a determination of the issue relating to temporary reductions in Panhandle's rates, apparently the Examiner interpreted the Commission's rejection of objections raised to the Staff motion therein as an indication of its tacit approval of such temporary rate reductions. In said *Panhandle* order the Commission stated:

"An interim order procedure as proposed by staff's motion is not unique to this Commission or other regulatory agencies. The Commission applied an interim order in *Illinois Commerce Commission v. Natural Gas Pipeline Co. of America, et al.*, 2 F.P.C. 218 (1940), 120 F.2d 625 (CA7, 1941), affirmed 315 U.S. 575. Courts have upheld other interim orders issued by this Commission. In particular see *Panhandle Eastern*

Pipe Line Co. v. F.P.C., 236 F.2d 606 (CA3, 1956). See also *State Corp. Commission of Kansas v. F.P.C.*, 206 F.2d 690 (CA8, 1953), certiorari denied 346 U.S. 922, rehrg. denied 347 U.S. 1022. For use of the interim order procedure by a state regulatory agency see *Houston Chamber of Commerce v. Railroad Commission*, PUR 1930B, 388 19 S.W. 2d 583 (Court of Civil Appeals, Texas, 1929). The Interstate Commerce Commission in its *ex parte* rate increase proceedings utilizes procedures closely analogous to those proposed in staff's motion, e.g., *Ex Parte* No. 175, 281 I.C.C. 557; *Ex Parte* No. 168, 272 I.C.C. 695; *Ex Parte* No. 206, 299 I.C.C. 429."

It is submitted that *these citations are not controlling in the circumstances of the instant case.*

A reading of the first three cases which are the only ones cited that arose under the Natural Gas Act clearly indicates important distinctions which make them inapposite herein:

5589

(1) The interim orders in those cases were "final" in the sense that they were not susceptible to retroactive adjustment by a subsequent order.

(2) No allocation issues were involved;

(3) The parties having rights determined by the interim orders had just had their "day in court" and a final determination of those issues.

In addition there are particular distinguishing elements of these cases which render them inapposite for the instant controversy.

Illinois Commerce Commission v. Natural Gas Pipeline Co. of America, et al; sub nom. F.P.C. v. Natural Gas Pipe-

(5589)

line Co. (1942) 315 U.S. 575. This case arose under Section 5 of the Natural Gas Act so that the interim rate order was *prospective* in effect and no refund was involved.

Moreover, at pages 584-585, the Court said:

"The first prerequisite to an order by the Commission is that it shall be preceded by a hearing and findings. In this case, while the proceedings were not ended by the interim order, the companies had full opportunity to offer all their evidence both direct and in rebuttal, and full opportunity to cross-examine every witness offered. . . . All the evidence tendered was received and considered by the Commission, and before the interim order was entered counsel for the companies stated to the Commission that they had concluded the direct testimony in support of their case."

Thus, where litigants are contesting one of the basic steps prerequisite to setting rates in various zones, and a "full hearing" has been denied, this case is not authority for an interim refund order.

5590

Panhandle Eastern Pipe Line Corporation v. F.P.C., (1956 CA 3) 236 F.2d 606.

This rate case was heard on a presentation of Panhandle's direct evidence immediately *subsequent* to a *final* determination on contested issues. The Commission was permitted to stand on its prior order because it "found that no new or supervening occurrences had been shown by Panhandle to warrant reconsideration of the commission's recent conclusions with reference to these matters." (p. 608)

In the instant case, however, there is no prior Commission order determining the contested cost allocation issue

(5591)

after a full hearing. If anything, it is submitted that the record in Docket No. G-11980, militates against the Staff's interim commitment to Tennessee's method of cost allocation as a basis for rate refunds.

State Corp. Commission of Kansas v. F.P.C. (1953 CA 8) 206 F.2d 690. (*Northern* case).

This was a rate case similar to the *Panhandle* case, *supra*, wherein an interim order was permitted because certain contested issues were disposed of in an immediately preceding case.

It is important to note that at page 713 the Court said:

"Whether or not appropriate opportunity to explore the problem of zone rates for *Northern* is presented in Docket No. G-1881, it is clear that the proponents of zone rates have made no record in this case to afford a basis for the establishment of such rates."

Contrast this failure of the zone rate proponents in the *Northern* case, with the Examiner's preclusion of the preparation and presentation of evidence of cost allocation by the parties in the instant case.

5591

Houston Chamber of Commerce v. Railroad Commission, PUR 1930B, 388, 19 SW 2d 583.

This case is inapposite to the problem presented by the Staff motion. The *Houston* case arose under a state statute which provided for Commission-initiated rates which "are conclusively presumed to be just, reasonable, and non-discriminatory until attacked in a direct proceeding authorized by statute for that purpose." (page 394) Moreover, these State Commission orders are specifically prospective in operation.

(5591)

Contrasted with this is the *Tennessee*-initiated rates which have no statutory presumption of reasonableness, and which are under attack.

Finally, the three I.C.C. cases cited are essentially not in point. Although captioned as *ex parte*, there were actually full hearings and interested parties participated fully in the development of the record. Furthermore, orders in such cases operated prospectively only. There was no requirement that refunds be made subject to a probable future retroactive determination that such refunds should have been made in a different manner. Untried issues were not prejudged. There was no confiscation or denial of due process.

3. *An Interim Refund Order Would Be an Abuse of the Administrative Process Herein.*

As long ago as its order issued October 6, 1955, in Docket No. G-5259, the Commission recognized that "the question of possible unlawful rates between zones is a relevant issue" and that "the charges of unjustness in the rates as between zones require a thorough and exhaustive study to

5592

determine . . . what method of allocating costs between zones would be fair and equitable to all concerned, in order that just and reasonable rates may be prescribed for each zone."

A subsequent order issued September 5, 1957, in the same docket stated that "the zoning issue can now be most clearly analyzed and presented in Docket No. G-11980."

Subsequent orders in Docket No. G-11980 quoted above make it clear that the Commission desires the cost allocation controversy to be decided in principle and method in

Docket No. G-11980 and that decision binding in future cases unless changed circumstances are shown.

It is the position of Columbia Companies in *Docket No. G-11980* that an Examiner's decision is required as a matter of law on the issue of cost allocation.* Obviously, then, if the Examiner's decision on this issue cannot be *waived* in *Docket No. G-11980*, the same issue cannot be ignored completely in *Docket No. G-11983*.

It is submitted that the Commission is bound by its decision to decide the allocation controversy in *G-11980* and any procedural shift (such as an interim refund order) which would undercut or prejudice Columbia Companies which have abided by the Commission's prior rulings is an abuse of the administrative process. (Cf. *Trunkline Gas Co. v. F.P.C.* (1957 CA3) 247 F2d 159)

5593

III. IF AN INTERIM REFUND ORDER IS ISSUED, THE COMMISSION SHOULD PROTECT COLUMBIA COMPANIES FROM THE ADVERSE EFFECTS OF UNDERCOLLECTIONS BY TENNESSEE FROM OTHER CUSTOMERS.

One fundamental evil of the interim *refund* procedure* is that a subsequent determination of the cost allocation issue, contrary to the Tennessee method, may entail substantial undercollections by Tennessee from certain customers. Thus, if Tennessee is permitted a specific overall rate of return in the initial piecemeal determination, Tennessee would either have to absorb its undercollections in

* See Columbia Companies' Answer dated May 27, 1960, to Motion of Consolidated Natural Gas System, pages 9-11.

* Columbia Companies are not opposed to interim *orders per se*. In fact the recent history of Tennessee rate proceedings shows several attempts to separate certain issues for trial and determination. However, these did not entail refunds.

(5593)

certain zones, and at the same time, necessarily recover less than the allowable return, or else, other customers would subsidize Tennessee's undercollections.

Since, generally, Tennessee uses the same zonal cost allocation formula in G-19983 as it did in G-11980, it is clear that the issue of substantial undercharges in certain zones still exists. Therefore, Columbia Intervenor's oppose any piecemeal rate reductions which would aggravate such undercharges to those zones and would require the Commission to determine Tennessee's rates and refunds to Columbia Intervenor's in a prejudicial context.

Columbia Intervenor's want it to be made clear that if *the Commission indulges in piecemeal reduction of Tennessee's rates, after determining that there is an improper dollar amount in some item of Tennessee's cost of service, such a piecemeal rate reduction in zones of services on some basis*

5594

other than that resulting from the final determination of the zoning question in G-11980 could not properly bar the Commission from granting full refunds to Columbia Intervenor's after the cost allocation issue is finally decided in Docket No. G-11980 and carried forward into this docket.

If the Commission would permit Tennessee to recoup its full cost of service even though there were undercollections from certain zones or classes of service, it is plain that the other zones and classes of customers, such as Columbia Intervenor's, would be subsidizing or "picking up the tab" for those customers who were undercharged. The allocation issue would be prejudged without any evidence and they would be denied due process of law.

Finally Columbia Intervenor's observe that several interim final orders in various issues in this case, without

(5595)

finally disposing of the whole proceeding, are susceptible to a duplication of trial issues and, potentially, a multiplicity of judicial reviews. Thus, instead of simplifying and expediting this proceeding, the exact opposite would occur.

WHEREFORE, Columbia Companies respectfully request that the Commission issue its order on the Motion of Staff Counsel which would:

(1) determine the fair overall rate of return for Tennessee in Docket No. G-11983, and any *subsequent* rate filing where no substantial change in circumstance is shown;

5595

(2) omit the intermediate decision procedure on this isolated issue;

(3) deny the request for an interim refund order.

Respectfully submitted,

BROOKS E. SMITH

Brooks E. Smith

Attorney for

The Manufacturers Light and
Heat Company

The Ohio Fuel Gas Company

United Fuel Gas Company

(5595)

Of Counsel:

BROOKS E. SMITH

JAMES G. O'NEILL

120 East 41st Street
New York 17, New York

Attorneys for

The Manufacturers Light and Heat Company

The Ohio Fuel Gas Company

United Fuel Gas Company

WILLIAM ANDERSON

JOHN P. EGAN, JR.

800 Union Trust Building
Pittsburgh 19, Pennsylvania

Attorneys for

The Manufacturers Light and Heat Company

W. F. LAIRD

RALPH N. MAHAFFEY

99 North Front Street
Columbus 15, Ohio

Attorneys for

The Ohio Fuel Gas Company

R. K. TALBOTT

HERBERT W. BRYAN

Post Office Box 1273
Charleston 25, West Virginia

Attorneys for

United Fuel Gas Company

Dated: June 13, 1960

626a In United States Court of Appeals for the Fifth
Circuit

No. 18547

TENNESSEE GAS TRANSMISSION COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

No. 18597

MANUFACTURERS LIGHT & HEAT COMPANY, THE OHIO FUEL
GAS COMPANY, UNITED FUEL GAS COMPANY, PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT

Transcript of hearing

October 19, 1960

[File Endorsement Omitted.]

Members of the Court present: Hon. Richard T. Rives,
Chief Judge; Hon. Elbert P. Tuttle, U.S. Circuit Judge; Hon.
John M. Wisdom, U.S. Circuit Judge.

626b

APPEARANCES

For Petitioner Tennessee Gas Transmission Com-
pany: Harry Littman, Jack Werner, and Harold Talisman,
Esqs., of counsel.

For Petitioners Manufacturers Light & Heat Company, The
Ohio Fuel Gas Company, United Fuel Gas Company: Brooks
E. Smith, Esq.

For Respondent: Peter H. Schiff, Esq.

For the City of Pittsburgh: David Stahl and Hurzel Plaine,
Esqs.

626c COLLOQUY BETWEEN COURT AND COUNSEL FOR
RESPONDENT

Judge RIVES. The thing that worries me about our position, or your position, Mr. Schiff, is that it seems to me you are asking us to let rates go into effect, a reduction in rates, tentative reduction, even this will not be a legally prescribed rate, it will be subject to change later on, and when all of the elements that go into the rate-making have not been passed on administratively. That is something that I didn't understand had occurred in any of these other interim orders that you cited. It seems to me that all of the elements probably that went into the rate-making had been passed on administratively, but I may be mistaken there.

Mr. SCHIFF. I believe if you examine these cases you will find that the procedure applied in these cases is precisely the same as involved here.

Judge RIVES. Did you have the allocation of cost problem?

Mr. SCHIFF. No, I concede there was no question of rate design. I would like to read in a minute a quote from the Panhandle case to indicate that this is not the only area where there may be variations and the result may be that a
626d company after an interim rate order may not obtain its full cost of service that might be permitted if it had filed the proper rate.

Now, in our response, the three cases we cite, I didn't give the page citations and it might be convenient if you would take those; it is on page 4 of our response, it is the Natural Gas Pipeline case, Supreme Court case. The pages of particular interest are 583 to 584.

Judge TUTTLE. Give us the volume, too.

Mr. SCHIFF. 315 U.S. The case starts at page 575.

Judge WISDOM. 583?

Mr. SCHIFF. That is right. I believe the appropriate page citation in the State Corporation of Kansas case, 206 Federal 2nd, is already in our response; and in the Panhandle Eastern case, which is 236 Federal 2nd, at page 666, the most pertinent pages are pages 608 to 609.

Now, the Natural Gas Case, which the Supreme Court decided in 1942 at very near the beginning of the regulation un-

der the Natural Gas Act, what the Commission did there, as here, it accepted the company, the Natural Gas Pipeline had presented all of its evidence, as I read the case. The Commission, for the purposes of that order, accepted a portion of the presentation of the Natural Gas Pipeline Company. This is what we have done here. We have accepted Tennessee's case, the basis on which they proposed to increase rates, in 626e their entirety, except as to the rate of return issue on which we have given a full hearing.

And the Natural Gas cases, the same thing was done, and as we point out in our response, the Supreme Court indicated that a party cannot complain about the fact that we have accepted the case that they asked us to accept.

Judge TUTTLE. Are you saying in effect that if it turns out that New England rates that are being charged or would be charged in order to get a yield or return of 6½ per cent are ultimately found to be too high—

Mr. SCHIFF. Too low, I think.

Judge TUTTLE. No, let me see, too high, and it should be lower and that a higher rate should be charged in the Eastern Zone and a lesser rate should be charged in the New England zone, that the company can't complain because the company fixed that rate, initially proposed that rate, and it is presumed to have done it correctly and if it hasn't done it correctly, it is their fault and nobody else's fault?

Mr. SCHIFF. That is precisely our position.

Judge TUTTLE. There is no guarantee that the rates that they proposed will actually yield 6.8 per cent?

Mr. SCHIFF. That is precisely our position.

Judge RIVES. Is that position good?

Mr. SCHIFF. Yes, sir.

Judge RIVES. Don't they have to take a pretty good 626f guess as to what the allocation of costs is going to be and aren't these local people in the zones more concerned with that than the parent company here, than the Tennessee Company?

Mr. SCHIFF. As to the last supposition, I am not sure. I think that the Pipeline Company does have some interest. It isn't merely a stakeholder. I think the rates it has in effect in particular zones may affect the sales it may be able to make in those zones.

But passing that, the situation in this case is no different than any other rate case. Now, under the Natural Gas Act the proponent of a rate files that rate. The Commission may suspend it and after five months it will go into effect subject to refund if the Commission so orders, that is a legally prescribed rate. They can't charge any other rate.

Now, taking the example that Mr. Littman gave to you before on its \$12 million, saying that they supposedly had a \$12 million increase, well, our point, position is this, even if we accepted, the company comes in and says we need \$12 million more than we have been collecting up to now, the Commission says, "Yes, that is correct, we agree with you," and even if we accepted a total cost of service, we may still determine, however, that they have been collecting too much in one zone and too little in another zone, so that the consequences that Tennessee ascribes to our order or to the 626g interim order are simply the consequences present in every rate case. And what Tennessee is asking here, and more precisely the Columbia System is asking here, is that even if the commission is right on the 7 per cent, even though the Commission is perfectly right that those rates are too high, that they are unjust and unreasonable, still we have to be allowed to charge our customers unjust and unreasonable rates until every other issue is determined.

May I say the situation would be the same if Tennessee had filed a rate based on a rate of return of 10 per cent or 50 per cent, it would be exactly the same thing. They would be claiming that we can collect padded rates until the whole case is finished. And we suggest that in determining whether or not to grant a stay, that the whole rate-making process can be undercut if either the Commission or the Courts were to grant a stay automatically in every case, regardless of how little merit there is to the position on the merits.

026h Mr. SCHIFF. The suggestion here is that in some way
that the interim rate cases we have cited can be dis-
626i tinguished because the allocation question or the rate de-
sign question is still pending. Comparable suggestions
seem to have been made in the Panhandle case, 236 Federal
2nd, and there the Court said at page 608, I have already
given you the page citation, I am only reading part of their
quote, but they say, "Panhandle must have based its claim
for higher rate of return upon justification existing at the
time of filing. It is difficult to see how else a change could
have been proposed in good faith. True, in recognition of the
time involved in these often long, drawn out rate proceedings,
the Commission quite properly permits the basic showing of
the justification which existed at the time of the filing to be
supplemented by evidence of occurrences since filing. But this
is far from saying that a party who tries and fails to make out
a prima facie showing to support several elements of his claim
is entitled to postponement of adjudication thereon in antici-
pation of possibly new justification which some future event
may supply before the overall case can be completed."

This we say is precisely the situation here. Tennessee is
saying we have filed rates based on 7 per cent. All right, maybe
we can't justify them. In the other phase of the case they
claim we are wrong on that, but maybe they say we can't
justify it, but that maybe at the end of the case after our
opponents have presented evidence, or even after the
626j staff have presented evidence, maybe then we can justify
evidence, and therefore in the meantime we have to be
able to collect rates which we cannot now on our own terms
justify.

We say that this motion is totally untenable and that Ten-
nessee has not made any showing that there is a likelihood
that they may prevail and that these earlier cases are full
justification for the interim rate procedure in this case.

632

FPC V. TENNESSEE GAS, TRANSMISSION CO.

630

In United States Court of Appeals for the Fifth Circuit

No. 18547

TENNESSEE GAS TRANSMISSION COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

No. 18597

THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE
OHIO FUEL GAS COMPANY, UNITED FUEL GAS COMPANY,
PETITIONERS.

v.

FEDERAL POWER COMMISSION, RESPONDENT

PETITIONS TO REVIEW ORDERS OF THE FEDERAL POWER
COMMISSION

Order of the Court Denying stay pending review

October 28, 1960

Before RIVES, Chief Judge, and TUTTLE and WISDOM,
Circuit Judges

631

PER CURIAM: All of the Judges are of the opinion that the petitioners have not made a strong showing of any likelihood that this Court will invalidate the Commission's determination that 7% is higher than a fair rate of return for Tennessee Gas Transmission Company. Judges Rives and Tuttle are of the further opinion that the petitioners have not made a sufficient showing of any likelihood that any party

will suffer irreparable loss because Tennessee Gas Company's method of allocating costs among different zones may ultimately be successfully challenged.

The Motions for Stay Pending Review of the Rate Orders of the Federal Power Commission, are, therefore, Denied.

WISDOM, Circuit Judge, Dissenting:

In my opinion, it is unreasonable, if not unlawful, in this case, for the Commission to specify a rate of return for Tennessee Gas Transmission Company when at the time of issuing the order the Commission knows that there is a likelihood that the company cannot possibly realize the rate of return. Here, the determination of the rate of return is so dependent on the determination of the allocation of costs among the six zones Tennessee services that the two issues can not be separated.

632 The interim order requires Tennessee to make immediate refunds to all its customers, undercharged distributors as well as overcharged distributors. The Columbia companies, which operate in Zones 2, 3 and 4, contend that they bear such a disproportionate share of the costs of Tennessee's services that, in effect, they are subsidizing Tennessee's distributors in Zones 1, 5 and 6. Tennessee must now make refunds on the present allocation of costs. If Columbia's challenge to the allocation is successful, Tennessee will be required to make additional refunds to distributors in Zones 2, 3 and 4. But Tennessee will not be able to recover adequate costs of services from the undercharged distributors in Zones 1, 5 and 6. Tennessee, therefore, if Columbia is successful, will be unable to realize the rate fixed by the Commission as just and reasonable.

The allocation issue has been tried and briefed in another proceeding involving Tennessee. It is ripe for decision. I see no reason then for the Commission not to put the horse where he belongs—in front of the cart.

634 FPC V. TENNESSEE GAS TRANSMISSION CO.

668 In United States Court of Appeals for the Fifth
Circuit

No. 18547

[Title omitted.]

No. 18567

[Title omitted.]

ON PETITION FOR REHEARING ON MOTION FOR STAY WHICH WERE
DENIED BY ORDER DATED OCTOBER 28, 1960

Order denying rehearing on motions for stay.

Filed November 21, 1960

Before RIVES, Chief Judge, and TUTTLE and WISDOM, Circuit
Judges

PER CURIAM:

The petition of the Manufacturers Light and Heat Com-
pany, The Ohio Fuel Gas Company, and United Fuel Gas
Company for a rehearing on motions for stay denied October
28, 1960, is Denied.

Judge Wisdom Dissents.

670 In United States Court of Appeals

Minute entry of argument and submission

May 29, 1961.

[Title omitted.]

On this day this cause was called, and after argument by
Harry S. Littman Esquire, and Brooks E. Smith, Esquire for
petitioners, and Peter H. Schiff, Esquire, Attorney Federal
Power Commission, and Robert E. Jameson, Esquire, for Inter-
venor, was submitted to the Court.

671 In United States Court of Appeals for the Fifth Circuit

No. 18547

TENNESSEE GAS TRANSMISSION COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

No. 18597

THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO
FUEL GAS COMPANY, AND UNITED FUEL GAS COMPANY,
PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT

PETITIONS FOR REVIEW OF ORDERS OF THE FEDERAL POWER
COMMISSION

Opinion

August 2, 1961

672 Before TUTTLE, Chief Judge, CAMERON and WISDOM,
Circuit Judges

TUTTLE, Chief Judge: These two petitions for review of orders of the Federal Power Commission attack, from somewhat different points, interim orders finding a 6½% rate of return just and reasonable, and putting said rate of return into effect before resolving other issues touching on the allocation of costs between different zones of operation of Tennessee Gas Transmission Company. Generally the name "Tennessee" will be used interchangeably with petitioner, and the name "Columbia Companies" will be reserved to discuss the petition of Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company.

The history of the proceedings leading up to the orders complained of is taken almost completely from the statement in petitioner's brief. In using such statement we have, however, eliminated some expressions of opinion and explanatory statements:

Tennessee owns and operates a natural gas pipeline system extending in a northeasterly direction from its sources of supply in Texas and Louisiana through the States of Texas, Louisiana, Arkansas, Mississippi, Alabama, Tennessee, Kentucky, West Virginia, Ohio, Pennsylvania, New Jersey, New York, Massachusetts, New Hampshire, Rhode Island and Connecticut. The rates charged by Tennessee for the transportation of natural gas and sales for resale of natural gas in interstate commerce are subject to the jurisdiction of the Commission under the Natural Gas Act (15 U.S.C. 717-717w).

673 On October 5, 1959, Tennessee filed with the Commission, pursuant to Section 4(d) of the Natural Gas Act, schedules of rate changes designed to recover the increased cost of providing natural gas service. These schedules set forth the respective rates proposed by Tennessee for each type of service in each rate zone on the Tennessee system. The Tennessee system is divided into six rate zones, with rates differing among the zones to give effect to distance, as well as other factors.

By order issued November 4, 1959, the Commission ordered a hearing to determine the "lawfulness" of the rates which had been filed. Following a five-month period of suspension, the rates became effective April 5, 1960, subject to an undertaking by Tennessee, required by Commission order, to "refund at such times and in such manner as may be required by final order of the Commission, the portion of the increased rates found by the Commission in this proceeding not justified, together with interest thereon at the rate of 7 percent per annum."

Hearings commenced on February 2, 1960, and continued intermittently until recessed on May 25, 1960. During the course of the hearings, Commission Staff Counsel moved that the hearing be divided into two phases. He proposed that the first phase deal solely with the issue of rate of return, and the remaining issues be reserved for a later stage of the proceeding. Staff Counsel further proposed that upon completion of the first phase of the proceeding, the Examiner's decision be omitted; that the Commission issue a decision determining the fair rate of return for Tennessee; and that the Commission
674 issue an interim order requiring Tennessee to reduce its rates and make refunds, in the event the Commission concluded that the fair rate of return is less than claimed by Tennessee.

When Staff Counsel made his motion, there was pending before the Commission, in another proceeding involving Tennessee (Docket No. G-11980), an issue as to the proper method of allocating Tennessee's cost of service among its six rate zones and various services. By order issued April 30, 1959, in Docket No. G-11980, the Commission ruled that determination of the allocation issue should be expedited and, to that end, severed that issue for separate and prior hearing and determination in that case. At the time Staff Counsel made his motion, the allocation issue had been thoroughly tried and briefed and was before the examiner for decision. Additionally, the Examiner in the instant proceeding had ruled that the determination of the allocation issue in Docket No. G-11980 would govern the method of allocating Tennessee's cost of service in this case.

Since it contended that determination of the allocation issue was required in order to translate the cost of service into rates for the various zones and services, Tennessee filed a memorandum opposing the Staff's motion for an interim order on the ground, inter alia, that such order would be illegal unless the Commission simultaneously determined the allocation issue. On July 19, 1960, Tennessee filed a motion with the Commission requesting it to determine the allocation issue simultaneously with the issue of rate of return. By order issued August 5, 1960, the Commission denied Tennessee's motion.

On August 9, 1960, the Commission issued its order, herein sought to be reviewed, adopting the Staff's interim 675 order procedure. As stated above, by such order the Commission disallowed Tennessee's claim for a 7 percent return, fixed a 6½ percent rate of return, required Tennessee to file reduced rates retroactively to April 5, 1960, and required Tennessee to make refunds for the differences in rates collected since April 5, 1960. The Commission's order did not, however, make any determination as to the proper method of cost allocation which should be employed in allocating the reduced cost of service among the six rate zones on the Tennessee system. Nor did the Commission make a determination as to which of the various rates filed by Tennessee were unlawful, which rates should properly be reduced, or to whom refunds were lawfully due. Instead, the Commission left these questions open for later determination.

On August 29, 1960, Tennessee filed its application for rehearing which the Commission denied by its order issued Sep-

tember 27, 1960. On October 3, 1960, Tennessee filed its petition to review with this Court and simultaneously filed a motion for stay of the Commission's order. On October 28, 1960, this Court, with one Judge dissenting, denied the motion for stay.

Although Tennessee summarizes its extended specifications of error by placing them in five numbered paragraphs,¹ we discuss them under two headings:

676 (1) The rate of $6\frac{1}{8}$ percent was based on findings "unsupported by substantial evidence and is unreasonably low."

(2) The Commission erred in putting a rate less than 7 percent into effect by an interim order prior to determining whether the cost allocations between the six zones were lawful.

Considering first the $6\frac{1}{8}$ percent rate, we find that the Commission had before it a full record disclosing sufficient economic

¹ This summary is as follows:

"1. The Commission erred in allowing Tennessee an over-all rate of return of only $6\frac{1}{8}$ percent. Such rate of return is confiscatory, deprives Tennessee of property without due process of law in contravention of the Fifth Amendment of the Constitution of the United States, and constitutes discriminatory, arbitrary and capricious action against Tennessee.

"2. The $6\frac{1}{8}$ percent rate of return is based on findings unsupported by substantial evidence and is unreasonably low in that:

"a. It fails to yield a return on common book equity commensurate with returns being earned by enterprises having corresponding risks.

"b. It is unjustifiably less than the rate of return allowed by the Commission in its most recent decisions to pipeline companies having a more secure capital structure than Tennessee.

"c. It fails to provide the margin of safety over the cost of debt necessary to prevent the quality of Tennessee's senior securities from deteriorating and being downgraded.

"3. The Commission arbitrarily required Tennessee to reduce the rate of return on its natural gas production properties even though the Commission set for further hearing the issue of the rate of return to be allowed on such properties.

"4. The Commission erred in the computation of Tennessee's capital structure in failing to include as common equity capital the convertible preferred stock which was in the process of being converted into common stock, and in failing to include in the capital structure mortgage bonds which had been issued by a Tennessee subsidiary.

"5. The Commission illegally and arbitrarily set aside Tennessee's rates without deciding the cost allocation issue, which decision was necessary in order for the Commission to determine which, and to what extent, the individual zone rates filed by Tennessee were unlawful."

factors to permit it to determine what was a just and reasonable return. Both Tennessee and the Commission recognize that the standard and principles to be observed in testing the correctness of the Commission's findings are to be found 677 in the two cases: Bluefield Waterworks & Improvement Co. v. Public Service Commission of W. Virginia, 262 U.S. 679, 692, and Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591.

The petitioner greatly stresses the following language from the Hope case:

"* * * the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital. * * *"

Although the Commission does not counter by emphasizing any particular language of the opinion, we cannot overlook the following:

"* * * It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important. Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a presumption of validity. And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences. Cf. Railroad Commission v. Cumberland Tel. 678 & Tel. Co., 212 U.S. 414; Lindheimer v. Illinois Bell Tel. Co., supra, pp. 164, 169; Railroad Commission v. Pacific Gas & Electric Co., 302 U.S. 388, 401." 320 U.S. 591, 602.

In stressing the language, "The return to equity owners should be commensurate with returns on investments in other enterprises having corresponding risks," petitioner argues extensively from the tables showing average earnings of the ten major pipelines over an eight-year period ending with 1958 and for the 41 pipeline companies comprising the entire industry over a ten-year period ending in 1959. It also strongly

emphasizes the fact that the 6½ percent return will yield the lowest return on common stock equity for any of its years of operation.²

The weakness of this approach is twofold: (1) There is no basis for Tennessee's implied assumption that it or any of the pipeline companies are entitled to the same return on book equity which they have historically enjoyed. "A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally." *Bluefield Waterworks & Improvement Co. v. Public Service Commission*, supra, p. 893. (2) The Commission found that petitioner was not an "average" pipeline company but rather that it is one of the largest and soundest. It is thus a non sequiter for petitioner to argue that because the eight or nine year average return on common equity of a group of companies has been higher than 10.12 percent then that rate is not just and reasonable for Tennessee for 1960.

The Commission specifically stated that it did "give consideration to the evidence of the return on book equity of Tennessee as compared to the other major pipeline companies as a factor in fixing a return which is commensurate with returns on investments of other enterprises having corresponding risks." With the evidence touching on the returns on book equity of other major pipeline companies present in the record, we cannot find, as invited to do by petitioner, that this statement of the Commission is without foundation.

Petitioner strongly attacks the weight attributed by the Commission to the "earnings-price" ratios of Tennessee as bearing on its competition for the investor dollar. We think it clear that the Commission used such comparison to test the degree to which the investing public considered the return to be "commensurate" with other pipeline companies. Touching on this matter the Commission said, "Such data indicate that Tennessee enjoys a favorable and improving position in the money market in relation to the rest of the industry."

We have carefully analyzed the criticisms levelled by the petitioner on both the method used by it and its conclusions

² It is not disputed that the 7 percent overall return sought by Tennessee would have provided a 12.70% return on the book value of Tennessee's common equity capital or that the 6½ percent overall return would provide a 10.12 percent return on common equity.

explaining its reason for adopting the $6\frac{1}{8}$ percent rate of return, and we find them to be without substance on the record before us. Moreover, we find no merit in the contention that the

Commission erred, in the computation of Tennessee's capital structure, in failing to include as common equity capital the convertible preferred stock which was in the process of being converted into common stock and in failing to include in the capital structure mortgage bonds which had been issued by a Tennessee subsidiary. We consider the treatment given to these two items by the Commission as well within its discretionary powers.

We next come to the challenge of the Commission's applying the $6\frac{1}{8}$ percent rate of return to Tennessee's natural gas production properties before a determination was made as to whether a different rate of return was justified for these properties. The Commission answers this complaint in two ways. It says, first, that Tennessee did not distinguish, in its application for a 7 percent overall rate, between the rate of return it was entitled to receive on its production properties from the overall rate. We think this is not an adequate answer, because a larger return for production properties may well have been recovered under a 7 percent overall rate, whereas this might not be the case under a $6\frac{1}{8}$ percent overall rate if production properties were later found to be entitled to a higher rate of return. However, as to the second point urged by the Commission, we think it fully answers petitioner's contention. In allowing $6\frac{1}{8}$ percent rate of return, the Commission postponed for future consideration the treatment to be afforded substantial amounts received by petitioner through its treatment of federal income tax provisions for statutory depletion and intangible well-drilling costs. The Commission concluded that if Tennessee shows that it is entitled to a higher return on that part of its capital that is represented by production properties, this can be provided for when the Commission makes a final disposition of the treatment of the two tax benefits reserved for later consideration.

We next come to the complaint that the Commission could not legally enter the interim order denying the 7 percent rate of return and inviting the filing of new schedules based upon a $6\frac{1}{8}$ percent rate so long as there remained unresolved the

question whether the allocations of cost among the six zones of operation would ultimately be approved by the Commission.

A majority of the Court, with the writer of this opinion dissenting, concludes that the Commission could not legally effectuate its order requiring the $6\frac{1}{8}$ percent rate of return to be given effect until it had made its determination as to the proper allocation of cost of service among the several zones. The following part of the opinion, written by Judge Wisdom, and concurred in by Judge Cameron, becomes the Court's opinion touching on this phase of the appeal:

WISDOM, Circuit Judge: On April 30, 1959, in another proceeding involving Tennessee, in Docket No. G-11980, the Commission issued an order stating:

"It is our view that separate and prior hearing on the issues relating to the principles and methods to be applied toward allocation of costs among the zones on Tennessee's system and among the classes of service within the zones will aid in the disposition of this proceeding and may be of similar aid in disposition of proceedings in Docket No. G-17166."

682 The Examiner in this proceeding rules that the cost allocation as determined in Docket No. G-11980 would govern the allocation of service in this case. The cost allocation issue is ready for decision.

What the Commission in 1959 considered a reasonable and orderly sequence of proceedings seems equally reasonable and orderly now.³

The Commission's refusal to decide the cost allocation issue means that there is no basis for determining which of the filed rates in specific zones are unlawful, the extent to which individual rates should be reduced, or to whom refunds are due. Meanwhile, the effect of the interim order is to continue the alleged discriminatory differential in favor of Zones 1, 5, and 6, although the Columbia companies, operating in Zones 2, 3, and 4, for several years have been endeavoring to have the Commission determine a proper cost allocation among the zones. Tennessee will be injured, because it will not be able to recover adequate costs of services from the undercharged distributors in Zones 1, 5, and 6. For that matter, Tennessee would be

³ In Tennessee Gas Transmission Co., FPC Docket No. G-5259, the Commission issued an order holding that it would be "premature," "unfair" and "improper" to issue an interim order before determining pending allocation issues.

injured if it were entitled to an overall return of 7 percent on its investment. It will be injured in any case because of the retroactive effect that will follow from the Commission's belated determination of cost allocation. This effect works in favor of Tennessee's overcharged customers, who are entitled to refunds, but works against Tennessee since it may not recoup from undercharged customers. Tennessee, therefore, 683 will be unable to earn the return the Commission considers just and reasonable, no matter what that rate is.

It is true, of course, that the allocation of costs in all six schedules was made by Tennessee; that if these allocations are correct and are approved Tennessee will not be damaged; that the burden rests on the applicant to justify each rate increase. But conditions change, costs are not static, and rates are at best an educated guess. It seems that in filing rates a public utility should not be held, at its peril, to the requirement of foretelling the decision of the Commission on the correctness of the rates. The statute appears to have been designed on the assumption filed schedules will have to be adjusted. Lawful rates may be determined only after a full hearing; until the Commission fixes rates the utility is protected by being allowed to collect at the filed rate but under bond and subject to refund, and the consumer is protected by the refund of excess charges with 7 percent interest.

We question whether the hearing in which the cost allocation issues was excluded was the "full hearing" contemplated in Section 4(e) of the Act. We question whether the order, issued after a hearing in which the issue of cost allocation was barred, is a lawful order. It seems, too, that when the retroactive effect of the eventual determination of cost allocation makes it highly unlikely, if not impossible, for a utility to earn a "just and reasonable return," such an interim order lacks the weight and legal effect courts properly give to most orders of the Commission. Finally, regardless of the Commission's authority to issue the order, we hold that cost allocation among 684 zones is such an essential element in determining whether the filed rates are excessive that it is unreasonable and an abuse of discretion to issue an interim rate order before deciding a pending allocation issue ripe for decision.

PER CURIAM:

The Court concludes that the manner in which the foregoing opinions can be given effect is to approve the order of the Commission as to all matters dealt with by it in the challenged order except its decision that the order was to become effective prior to a final determination of the allocation issue, and except the order requiring immediate refunds of the excessive rates collected under the suspended schedules. The order of the Commission is in these respects set aside. The case is remanded to the Commission for further proceedings not inconsistent with this opinion.

Cameron, Circuit Judge, Concurs in the Result.

TUTTLE, Chief Judge, dissenting in part:

Although all members of the Court are in accord on the matters discussed in the main body of the opinion, I respectfully dissent from that part of the opinion that holds that the reduced rate of return cannot be legally effected by a Commission order until the Commission makes the determination of allocation of cost of service.

The significance of this issue is made apparent by the 685 petition of the Columbia Companies. This petition asserts that these companies have consistently opposed the schedules filed by Tennessee to be effective in zones 2, 3 and 4, in which they operated because, so they alleged, Tennessee had allocated its cost of service unfairly against their interests and in favor of zones 1, 5 and 6. It is asserted that by reducing the rate to be charged by cutting from 7 percent to 6 $\frac{1}{8}$ percent the rate of return, this would increase the amount by which zones 1, 5 and 6 are underpaying their proper rates. It is clear that if the Commission should later determine that cost allocations improperly favored zones 1, 5 and 6, the customers in those zones would be benefitted to the extent that they had obtained the gas at the rate now approved by the Commission's interim order. This follows from the structure of the statute which makes rate increases prospective only. In other words, there is no way in which Tennessee could hereafter, if we approve this 6 $\frac{1}{8}$ percent order, collect additional sums to make up for the advantage zones 1, 5 and 6 will have enjoyed because they were favored temporarily with a cost of service allocation improperly weighted in their favor.

Columbia's next contention, however, does not follow from

this fact. Columbia claims to be prejudiced because it says zones 1, 5 and 6 may subsequently be found to have received gas too cheaply at Columbia's expense. It is true that it is possible that the Commission may find that zones 1, 5 and 6 have received gas too cheaply. The weakness of Columbia's position, however, is that Columbia is not, and cannot be, hurt by any such subsequent determination. This follows because the rates which Columbia is now paying are still being paid subject to a final determination as to their lawfulness
686 as to all matters except the rate of returns on the common equity. Thus, it will be entitled to a refund of all amounts it may be found to have paid in excess of the correct rate because of an improper allocation of costs of service. Columbia is now immediately benefitted to the extent that it is paying, subject to refund, on schedules including a 6½ percent rather than a 7 percent rate of return. It is not an aggrieved party merely because the Commission did not proceed to a final determination of other possible savings to it at the same time.

The Columbia companies strongly argue that they are entitled under the statute, as an interested party, to a determination by the Commission of their complaint of undue preferences granted to the other zones in violation of Section 4(b) of the Natural Gas Act. They are undoubtedly entitled to such a determination, but not necessarily before the Commission can eliminate what it finds to be an unlawful increment in the price structure. See *State Corporation Com. of Kansas v. F.P.C.*, 8 Cir., 206 F. 2d 690, cert. den. 346 U.S. 922. Columbia could be hurt in these circumstances only if Tennessee were to be permitted to withhold refunds to which Columbia might become entitled on the ground that it could not recoup from zones 1, 5 and 6, and, therefore, it could not be required to refund excessive charges from zones 2, 3 and 4. As I will next show, this is not the law.

Tennessee claims that there is nothing in the Natural Gas Act that warrants the entry of an order that has the effect of reducing the charges it can make until the Commission decides whether it may not be charging too little from three
687 zones even though it may be charging too much in three others.

The Commission answers this in two ways: (1) the allocation of costs in all six schedules was made by Tennessee. If

these allocations are correct and are approved Tennessee will not be damaged. If they are incorrect they will be corrected and Tennessee will be required to make additional refunds to customers in those zones that were unfairly burdened by the improper allocations, but it will be unable to collect for any increased rates as such that a correct allocation would have warranted from the customers in the zones where there was an unfairly low increment of cost of service. This, the Commission says, is only the natural result of the regulatory scheme envisaged by the Natural Gas Act. The burden rests on the applicant to justify each rate increase. This includes the burden to establish the correctness of the allocation of costs of service as to each schedule filed. Tennessee stands in no different position than if the Commission, after the section 4 hearing, decided that Tennessee was entitled to an overall return of 7 percent on its investment, just as asked for by Tennessee, but decided that the cost allocations between the several zones were discriminatory, as here claimed by Columbia. The Commission would not have the authority to increase the schedules filed by Tennessee in zones 1, 5 and 6, but it would be under the obligation to reduce those for 2, 3 and 4 and make refunds for excess amounts paid by Columbia. See *Interstate Power Co. v. Federal Power Com.*, 8 Cir., 236 F. 2d 372. In such a situation Tennessee would not realize the full permitted rate of return because it would have failed to substantiate the correctness of the cost allocation. Of course, the Commission could, and should under such circumstances, authorize the filing of new schedules to have prospective effect to remedy the allocation imbalance, but it would have no power to authorize Tennessee to collect more from zones 1, 5 and 6 than its filed schedules called for. (2) The Commission has a second answer to Tennessee's criticism in this regard. It seems to say that Tennessee still has several unresolved rate increases pending, all of which affect these same zones, and, if Tennessee is found to have undercharged zones 1, 5 and 6, it may have ample funds collected under bond subject to refund to customers in these zones from which it can recoup for a failure to charge the permissible rate for the period of this present rate proceeding. I think we need not speculate on this matter because I think the first contention elaborated above is sound.

I would affirm the Commission's order in full.

689 In United States Court of Appeals for the Fifth Circuit
October Term, 1960

No. 18547

TENNESSEE GAS TRANSMISSION COMPANY,
PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

No. 18597

THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO
FUEL GAS COMPANY, AND UNITED FUEL GAS COMPANY,
PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT

PETITIONS FOR REVIEW OF ORDERS OF THE FEDERAL POWER,
COMMISSION

Before TUTTLE, Chief Judge, CAMERON and WISDOM, Circuit
Judges

Judgment

August 2, 1961

These causes came on to be heard on the petitions of Tennessee Gas Transmission Company and The Manufacturers Light and Heat Co., The Ohio Fuel Gas Company, and United Fuel Gas Company, for review of orders of the Federal Power Commission issued on August 9, 1960 and September 27, 1960 in Docket No. G-19983, and was argued by counsel;

On consideration whereof, It is now here ordered, adjudged and decreed by this Court that the orders of the Commission in these causes be, and the same are hereby, approved in part and set aside in part in accordance with the opinion of this Court; and that these causes be, and they are hereby, remanded to the Commission for further proceedings not inconsistent with the opinion of this Court.

"Cameron, Circuit Judge, concurs in the result."

"Tuttle, Chief Judge, dissents in part."

AUGUST 2, 1961,

Issued:—

690 In the United States Court of Appeals for the
Fifth Circuit

No. 18547

[File endorsement omitted.]

[Title omitted.]

No. 18597

PETITIONS FOR REVIEW OF ORDERS OF THE FEDERAL POWER
COMMISSION

Order denying petition for rehearing

October 5, 1961

Before TUTTLE, Chief Judge, CAMERON and WISDOM, Circuit
Judges

PER CUREAM:

It is Ordered that the petition for rehearing filed in the above
styled and numbered cause be, and the same is, hereby Denied.

Tuttle, Ch. J., Dissenting.

691 In United States Court of Appeals for the Fifth Circuit

[File endorsement omitted.]

[Title omitted.]

Order staying mandate

October 25, 1961

On consideration of the Application of the Respondent in
the above numbered and entitled causes for a stay of the
mandate of this court therein, to enable Respondent to apply
for and to obtain a writ of certiorari from the Supreme Court
of the United States, It Is Ordered that the issue of the man-
date of this court in said causes be and the same is stayed to
and including November 19, 1961; the stay to continue in

force until the final disposition of the case by the Supreme Court, provided that within that time there shall be filed with the clerk of this court the certificate of the clerk of the Supreme Court that certiorari petition and record have been filed. It is further ordered that the clerk shall issue the mandate upon the filing of a copy of an order of the Supreme Court denying the writ, or after November 19, 1961, unless the above-mentioned certificate shall be filed with the clerk of this court within that time.

Done at New Orleans, La., this 25th day of October 1961.

ELBERT P. TUTTLE,

United States Circuit Judge.

694 In United States Court of Appeals for the Fifth Circuit

[File endorsement omitted.]

[Title omitted.]

Order further staying mandate

November 15, 1961

On Consideration of the Application of the Respondent in the above numbered and entitled causes for a further stay of the mandate of this court therein, to enable Respondent to apply for and to obtain a writ of certiorari from the Supreme Court of the United States, It Is Ordered that the issue of the mandate of this court in said causes be and the same is further stayed to December 11, 1961; the stay to continue in force until the final disposition of the case by the Supreme Court, provided that within that time there shall be filed with the clerk of this court the certificate of the clerk of the Supreme Court that certiorari petition and record have been filed. It is further ordered that the clerk shall issue the mandate upon the filing of a copy of an order of the Supreme Court denying the writ, or after December 11, 1961, unless the above-mentioned certificate shall be filed with the clerk of this court within that time.

Done at New Orleans, La., this 15th day of November 1961.

ELBERT P. TUTTLE,

United States Circuit Judge.

[File endorsement omitted.]

IN THE MATTER OF TENNESSEE GAS TRANSMISSION COMPANY

Answer and objections of New England zone companies to Tennessee Gas Transmission Company's motion to omit intermediate decision procedure on issue of cost allocation

Filed July 29, 1960

Come Now

The Berkshire Gas Company
Blackstone Valley Gas and
Electric Company
The Bridgeport Gas Com-
pany
Central Massachusetts Gas
Company
Concord Natural Gas Corpo-
ration
The Connecticut Gas Com-
pany
Fitchburg Gas and Electric
Light Company
Gas Service, Inc.
The Greenwich Gas Company
The Hartford Electric Light
Company
Haverhill Gas Company
City of Holyoke, Massachu-
setts Gas and Electric De-
partment

The Housatonic Public Serv-
ice Company
Lawrence Gas Company
Lowell Gas Company
Lynn Gas Company
Manchester Gas Company
Mystic Valley Gas Company
The New Britain Gas Light
Company
North Shore Gas Company
Northampton Gas Light Com-
pany
Springfield Gas Light Com-
pany
Wachusett Gas Company
City of Westfield Gas and
Electric Light Department
Worcester Gas Light Com-
pany

(the New England interveners) and, pursuant to Section 1.12(c) of the Commission's Rules of Practice and Procedure, file their Answer and Objections to the Motion filed by Tennessee Gas Transmission Company (Tennessee) in which it urges the Commission to omit the intermediate decision procedure on the zone allocation issue presented in Docket No.

G-11980 and to decide the zone allocation issue in that docket simultaneously with the rate of return issue in Docket No. G-19983. The New England interveners respectfully request the Commission to deny said Motion for the following reasons:

697 1. Tennessee failed to file the Motion within the time required by Section 130(c)(3) of the Commission's Rules of Practice and Procedure.

2. The Commission would benefit from a decision by the Presiding Examiner who heard the testimony presented and who is now familiar with the various basic zone allocation methods proposed.

3. Omitting the Presiding Examiner's decision would probably not, as a practical matter, expedite a final determination of the zone allocation issue.

MOTION NOT TIMELY FILED

Section 130(c)(3) requires that "Requests for waiver and omission of the intermediate decision procedure shall be by motion filed with the Commission at any time during, *but not later than five days next following*, the conclusion or adjournment *sine die* of the hearing * * * [Italics supplied]."

Hearings on the zone allocation issue in Docket No. G-11980 were concluded on December 17, 1959. As the Presiding Examiner stated on the last day of the hearing " * * * the hearing of the zone phase of this proceeding its concluded" (Tr. 9170). Briefing dates were set at that time and initial and reply briefs have since been filed. By order dated April 30, 1959 in Docket No. G-11980, the Commission had severed the cost of service issue from the zone allocation issue so that the latter could be heard and decided independently.

698 Inasmuch as this Motion is directed to the sole issue of zone allocation and since it is clear that the hearing is concluded on this issue and that no further hearings will be scheduled, the five (5) day period specified in Section 130(c)(3) of the Commission's Rules should be considered as running from December 17, 1959, the last day of the hearing on this issue. Manifestly, Tennessee's untimely filing of this Motion more than seven (7) months after the time specified by the Commission's Rules for such a motion would, in and of itself, require denial of the procedure requested

THE COMMISSION WOULD BENEFIT FROM A DECISION BY THE
PRESIDING EXAMINER

The record to date in Docket No. G-11980 covers 9,170 pages of transcript and more than 140 exhibits. Substantially more than half of this record is applicable to the zone allocation issue. This material was presented by the Applicant, the Staff and various interveners over a period of approximately three years and has required a prodigious amount of time, energy and expense of each of the parties. We agree that the time for decision is here. The question now to be considered by the Commission is whether omission of a decision by the Presiding Examiner would be in the best interests of all concerned, and particularly in the best interest of the consuming public.

The Presiding Examiner in this proceeding, by reason of his function at the hearing, became familiar with both the testimony and exhibits as they were presented and, therefore, is already conversant with the various basic zone allocation methods proposed. His presence at these hearings permitted him to make specific inquiries of the witnesses whenever he felt clarification was needed. Consequently the Presiding Examiner has been able to obtain a comprehensive grasp of the highly technical aspects of this zone allocation issue and, from first hand observation of the witnesses' presentation, to gain a valuable insight into the relative validity of the conflicting allocation methods. In view of these facts, the New England interveners believe that a decision by this Presiding Examiner would prove to be of great help and value to the Commission. Undoubtedly, the Presiding Examiner's decision would point up the issues in conflict between the respective parties. Furthermore, any exceptions to his decision filed by the parties would bring into still sharper focus the areas of conflict. Most assuredly the Commission itself could perform the tasks and function of the Presiding Examiner, but we submit that the circumstances of this case make it most desirable to have an initial decision by the Examiner who presided throughout this lengthy and most complex trial.

In Tennessee's Motion, Page 2, it is suggested that the omission of the Presiding Examiner's decision "would serve the best interests of all concerned." We do not agree with this statement. As pointed out previously, we believe that the Presiding Examiner's decision would be of such value to the

ultimate determination of this issue as to be clearly in the best interests of all concerned. Furthermore, the fact that simultaneous decisions of both the zone allocation and rate of return issues might obviate certain "risks" of Tennessee does not constitute a suitable or valid reason for granting its
700 Motion in view of the loss to the general public which would result from omission of the Presiding Examiner's decision.

OMITTING THE PRESIDING EXAMINER'S DECISION MAY NOT, AS A PRACTICAL MATTER, EXPEDITE A FINAL DETERMINATION OF THE ZONE ALLOCATION ISSUE

There is no doubt that all the parties to this proceeding are equally desirous of expediting a final determination of the zone allocation issue as well as the other issues in Tennessee's three pending rate cases (Docket Nos. G-11980, G-17166 and G-19983). What we are here concerned with is the most effective procedure to reach this mutually agreed upon goal.

Apart from the fact that the New England intervenors consider the Presiding Examiner's decision as being of value and essential to the final determination of the zone allocation issue, we believe that as a practical matter omitting this decision would not expedite the case. Assuming that the Presiding Examiner has not as yet begun his final review of the material presented, he at least has had an initial exposure at the time of the hearing sessions to all such material and is familiar with the various basic zone allocation method proposed. It would seem reasonable to conclude that a person in such a position would be able to complete a review of the material relating to the various proposed zone allocation methods considerably quicker than an individual who has not heard the evidence as it was presented. Furthermore, in view of the heavy work load now being carried by the Commission, we submit that a

more reasonable approach would be to follow the normal procedure and permit the Presiding Examiner to
701 prepare his decision subject to review by the Commission. In contrast to the tremendous amount of time which would be required of the Commission to review this case (essentially in its entirety) and prepare its decision, the time required to review the Presiding Examiner's decision in the light of the exceptions taken thereto would be relatively small. Under the

circumstances, therefore, we submit it is most doubtful that the Commission's decision could be rendered any earlier by eliminating the assistance which the Presiding Examiner is able to provide in this case. Accordingly, even from a time point of view, the New England interveners believe the interests of all concerned would be best served by permitting the Presiding Examiner to review the material presented and prepare the initial decision.

In conclusion, we further submit there is no reason why the Commission's decision on the rate of return issue (which can be rendered promptly) should be delayed for the substantial period of time it would take the Commission to reach a decision on the zone allocation issue.

702 Wherefore, the New England interveners request that Tennessee's Motion be denied in its entirety.

Respectfully submitted.

The Berkshire Gas Company
Blackstone Valley Gas and
Electric Company

The Bridgeport Gas Company
Central Massachusetts Gas
Company

Concord Natural Gas Corpora-
tion

The Connecticut Gas Com-
pany

Fitchburg Gas and Electric
Light Company

Gas Service, Inc.

The Greenwich Gas Company

The Hartford Electric Light
Company

Haverhill Gas Company

City of Holyoke, Massachu-
setts Gas and Electric De-
partment

The Housatonic Public Serv-
ice Company

Lawrence Gas Company

Lowell Gas Company

Lynn Gas Company

Manchester Gas Company

Mystic Valley Gas Company

The New Britain Gas Light
Company

North Shore Gas Company

Northampton Gas Light Com-
pany

Springfield Gas Light Com-
pany

Wachusett Gas Company

City of Westfield Gas and
Electric Light Department

Worcester Gas Light Com-
pany

By (S) JOHN W. GLENDENING, Jr.,

Their Attorney.

JOHN W. GLENDENING, Jr.,

JOHN S. SCHMID,

300 Park Avenue, New York 22, N.Y.

Dated July 28, 1960.

713 Before the Federal Power Commission

Docket Nos. G-11980 and G-19983

IN THE MATTER OF TENNESSEE GAS TRANSMISSION COMPANY

Cross-motion to expedite and answer to motion to omit intermediate decision procedure on issue of cost allocation

Filed July 29, 1960

[File endorsement omitted.]

* The Ohio Fuel Gas Company, The Manufacturers Light and Heat Company, and United Fuel Gas Company (Columbia Companies) hereby answer and oppose the Motion of Tennessee Gas Transmission Company to Omit Intermediate Decision Procedure on Issue of Cost Allocation and renew their Motion to relieve Examiner Zwerdling of all other duties in order to expedite these proceedings.

On July 19, 1960, Tennessee Gas Transmission Company (Tennessee) filed a Motion to Omit Intermediate Decision Procedure on Issue of Cost Allocation, which is now pending before Presiding Examiner Zwerdling in Docket No. G-11980. In said Motion Tennessee recites that hearings on the issue of cost allocation were concluded on December 17, 1959, and briefing was concluded on April 11, 1960. In the course of the hearings in Docket No. G-19983, which have occupied a very substantial part of Examiner Zwerdling's time since briefs were submitted in G-11980, the Examiner observed that he had been unable to make any progress on his decision on the allocation issue due to the press of other matters. He estimated that his decision would not be issued until about November. Because of these facts Tennessee urged the Commission to omit the intermediate decision procedure.

714 Columbia Companies share Tennessee's concern over the delay of the decision in Docket No. G-11980. They believe that the decision on the allocation issue is much more urgent and important to Tennessee and to Tennessee's customers and the consuming public than the hearings in Docket No. G-19983, which have made it impossible for the Examiner to decide the prior case. The decision in G-11980 will affect the trial of Docket No. G-19983 to a very substantial degree. After the allocation issue is decided in

Docket No. G-11980, evidence must be presented in Docket No. G-19983 showing the effect of the approved allocation method upon costs in the latter case. On May 12, 1960, Columbia Companies filed a Motion to Expedite Proceedings, wherein they stated:

"F. On January 14, 1957, Tennessee Gas Transmission Company filed increased rates which were suspended by order in Docket No. G-11980 until July 14, 1957, at which time they became effective subject to refund. Such rates provided increased revenues of \$25,527,000 over the final rates in Tennessee's previous case, Docket No. G-5259, based on twelve months ended December 31, 1956. Of such increased revenues, \$8,355,000 was obtained from Columbia Companies.

"2. Hearings commenced in Docket No. G-11980 on April 16, 1957, and continued intermittently until December 17, 1959. Briefs were submitted on March 14, 1960, and reply briefs were submitted on April 11, 1960, relating to issues as to how Tennessee's costs should be allocated among its various zones and classes of customers. It should be noted that the Commission, by order issued April 30, 1959, severed the allocation issue and ordered that it be resolved first.

"3. On November 14, 1958, Tennessee filed another rate increase designed to produce \$19,184,000 of additional revenues of which \$4,802,000 would be obtained from Columbia Companies. Such rates were suspended by order in Docket No. G-17166 until May 15, 1959, at which time they were placed in effect subject to refund. No hearings have been set with respect thereto.

"4. On October 5, 1959, Tennessee filed another rate increase designed to produce \$26,864,000 of additional revenues, of which \$6,675,000 would be obtained from Columbia Companies. Such rates were suspended by order in Docket No. G-19983 until April 5, 1960, at which time they became effective subject to refund.

715 "5. Hearings commenced in Docket No. G-19983 on February 2, 1960, and were held intermittently for eleven days through April 12, 1960. The next hearing date is scheduled for May 24, 1960. To date, more than 1400 pages of transcript have been recorded on the single issue of rate of return. Examiner Zwerdling, who heard the evidence in Docket No. G-11980 and to whom briefs have been submitted, is also hearing the case in Docket No. G-19983. Even if some issues, such as rate of return, could be resolved quickly in

Docket No. G-19983, the ultimate effect upon rates depends upon the allocation issues to be resolved in Docket No. G-11980. Essentially, until the allocation issue which involves millions of dollars as between zones is resolved, the other issues cannot be finally resolved. The severance of the allocation issue in Docket No. G-11980 underlines the validity of this point.

"It is believed that if the allocation issue in Docket No. G-11980 were decided, many of the other issues in Tennessee's pending rate cases might be disposed of quickly by compromise and settlement.

"The issues now pending before Examiner Zwerdling in Docket No. G-11980 are very substantial and require the Examiner's careful attention. It is respectfully submitted that the Examiner cannot decide such case in a workmanlike manner while he is hearing evidence in other cases. It is further submitted that the trial of part of the issues in Docket No. G-19983 prior to the cost of service phase of Docket No. G-11980 and prior to Docket No. G-17166 will result only in confusion and further delay.

"Wherefore, in order to expedite the determination of the issues in the three pending Tennessee rate cases under which Columbia Companies are paying approximately \$20,000,000 per year, subject to refund, the Commission is respectfully urged to suspend hearings in Docket No. G-19983 until Docket No. G-11980 has been decided, and insofar as possible, to relieve Trial Examiner Zwerdling of further duties until he is afforded an opportunity to issue a decision in Docket No. G-11980."

By order issued July 1, 1960, the Commission denied said Motion, stating:

"It is our view that it would not be appropriate *at this time* to suspend the hearings in Docket No. G-19983. The Presiding Examiner is fully aware of the importance attached by the parties to the zone allocation issue and, without doubt, gave that matter full consideration in scheduling hearing sessions in Docket No. G-19983. We believe that the matter should be left to his discretion." [Emphasis supplied.]

716 Seventeen days of hearings have now been held in Docket No. G-19983, and oral argument on some of the issues is scheduled to be held before the Commission on

¹ This statement is in apparent conflict with the Commission's order setting Docket No. G-19983 for hearing.

July 29, 1960. Hearings are scheduled to reconvene on December 6, 1960.

Since the Examiner has refused to receive evidence with respect to the allocation of costs in Docket No. G-19983, because the allocation issue is pending on a complete record in Docket No. G-11980, any decision or interim decision in Docket No. G-19983 cannot be implemented until the allocation issue is decided in Docket No. G-11980. It is, therefore, respectfully submitted that the Commission should now suspend proceedings in Docket No. G-19983 until the allocation issue in Docket No. G-11980 has been decided. It is further requested that the Commission relieve Examiner Zwerdling of *all* other duties until his decision in Docket No. G-11980 has been issued. It is submitted that such action would greatly expedite the determination of all of the issues in all of Tennessee's pending rate cases and in numerous rate cases of its suppliers affecting millions of consumers.

During the hearings in G-19983, on July 11, 1960, Examiner Zwerdling stated that other duties had made it impossible for him to make any progress on the decision of the Tennessee zoning issue. (T. 2206) Tennessee then moved on July 19, 1960, to omit the intermediate decision procedure in Docket No. G-11980.

The intermediate decision procedure is of paramount importance in this case. The parties have literally spent years and hundreds of thousands of dollars developing a voluminous and complicated record² on the extremely important and seriously contested allocation issue. Examiner Zwerdling heard the testimony and has devoted many months of his time to this important issue. It would be impossible for the Commission to read this voluminous record. It would also be impossible for the Commission to properly evaluate all of the issues without first obtaining a decision by the Presiding Examiner. Millions of consumers have a vital interest in the decision of the allocation issue, and the omission of the intermediate decision would be highly prejudicial to them.

The question posed by Tennessee's Motion is whether Columbia Companies and others who have spent hundreds of thousands of dollars trying this issue on the basis of the facts

² Consisting of seventy volumes of transcript and 141 exhibits and numerous items which were incorporated by reference to the Commission's files.

shall be denied the benefit of Examiner Zwerdling's knowledge of the facts. Will their rights to due process become a formality devoid of substance?

Columbia Companies believe that due process is impossible in Docket No. G-11980 without an intermediate decision on the allocation issue. The Commission could not read, analyze and evaluate the evidence within a year. It is submitted that the assistance of its Staff would be prejudicial to Columbia Companies because the Staff has taken an adversary position in the proceeding.

It is respectfully submitted that the Examiner could decide the issues now pending before him in Docket No. G-11980 much more promptly than could the Commission if he were relieved of his other duties and given an opportunity to prepare a decision. It is further submitted that the Commission's failure to thus expedite the decision in Docket No. G-11980 is resulting in unnecessary and unreasonable delay in the determination of Tennessee's other rate cases and the rate cases of its customers. As heretofore pointed out in Columbia's Motion to Expedite Proceedings, many of the other issues in Tennessee's pending rate cases could probably be settled expeditiously by agreement of the parties and the Commission Staff if the allocation issue were first decided.

Wherefore, the Commission is respectfully urged to (a) suspend hearings in Docket No. G-19983 and relieve Examiner Zwerdling of all other duties until an intermediate decision in Docket No. G-11980 has been issued, and (b) deny Tennessee's Motion to Omit Intermediate Decision Procedure in Docket No. G-11980.

Respectfully submitted.

/s/ TILFORD A. JONES,
EDWARD B. CALLAND,

120 East 41st Street,
New York 17, New York.

Attorneys for:
THE OHIO FUEL GAS COMPANY,
THE MANUFACTURERS LIGHT
AND HEAT COMPANY, AND
UNITED FUEL GAS COMPANY.

Dated July 29, 1960.

660

EPC V. TENNESSEE GAS TRANSMISSION CO.

785

[Clerk's certificate to foregoing transcript omitted in printing.]

786

Supreme Court of the United States

No. 591, October Term, 1961

FEDERAL POWER COMMISSION, PETITIONER

v.

TENNESSEE GAS TRANSMISSION COMPANY, ET AL.

Order allowing certiorari

January 22, 1962

The petition herein for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit is granted. The case is consolidated with No. 605 and a total of two hours is allowed for oral argument.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

787

Supreme Court of the United States

No. 605, October Term, 1961

CITY OF PITTSBURGH, PENNSYLVANIA, PETITIONER

v.

TENNESSEE GAS TRANSMISSION COMPANY, ET AL.

Order allowing certiorari

January 22, 1962

The petition herein for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit is granted. The case is consolidated with No. 591 and a total of two hours is allowed for oral argument.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statute involved	3
Statement	3
Reasons for granting the writ	8
Conclusion	21
Appendix A	22
Appendix B	39
Appendix C	44

CITATIONS

Cases:

<i>Brooklyn Savings Bank v. O'Neil</i> , 324 U.S. 697	11
<i>Central States Co. v. Muscatine</i> , 324 U.S. 138	11
<i>Federal Power Commission v. Hope Natural Gas Co.</i> , 320 U.S. 591	10
<i>Federal Power Commission v. Interstate Natural Gas Co.</i> , 336 U.S. 577	11
<i>Federal Power Commission v. Natural Gas Pipeline Co.</i> , 315 U.S. 575	12
<i>Hope Natural Gas Co. v. Federal Power Commission</i> , 196 F. 2d 803	11
<i>Interstate Power Co. v. Federal Power Commission</i> , 236 F. 2d 372, certiorari denied, 352 U.S. 967	15
<i>Northern Natural Gas Co.</i> , 13 F.P.C. 1518	18
<i>Panhandle Eastern Pipe Line Co. v. Federal Power Commission</i> , 236 F. 2d 606	12, 13-14, 18
<i>Panhandle Eastern Pipe Line Co.</i> , 25 F.P.C. 787, 38 P.U.R. 3d 332, pending on review, C.A.D.C., No. 16583	14

Cases—Continued

<i>State Corporation Commission of Kansas v. Federal Power Commission</i> , 206 F. 2d 690, certiorari denied, 346 U.S. 922.....	12, 14, 18
<i>Sunray Mid-Continent Oil Co. v. Federal Power Commission</i> , 364 U.S. 137.....	10
<i>Tennessee Gas Transmission Co. v. Federal Power Commission</i> , 283 F. 2d 729.....	7
<i>United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division</i> , 358 U.S. 103.....	9
<i>United Gas Pipe Line Co. v. Mobile Gas Service Corp.</i> , 350 U.S. 332.....	9

Statutes and regulations:

Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821, as amended, 15 U.S.C. 717-717w:	
Section 4, 15 U.S.C. 717e.....	2, 8, 39
Section 4(a), 15 U.S.C. 717c(a).....	39
Section 4(b), 15 U.S.C. 717c(b).....	39
Section 4(c), 15 U.S.C. 717c(c).....	39
Section 4(d), 15 U.S.C. 717c(d).....	3, 40
Section 4(e), 15 U.S.C. 717c(e).....	9, 16, 20, 40
Section 5(a), 15 U.S.C. 717d(a).....	12, 41
Section 16, 15 U.S.C. 717o.....	42
Section 19(b), 15 U.S.C. 717r(b).....	2, 43

Federal Power Commission Rules of Practice and Procedure, 18 C.F.R. 1.30 (c)(3).....	5
--	---

Miscellaneous:

Federal Power Commission Annual Report for 1953.....	10
1 Sharfman, <i>The Interstate Commerce Commission</i> (1931).....	11

In the Supreme Court of the United States

OCTOBER TERM, 1961

No. —

FEDERAL POWER COMMISSION, PETITIONER

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, AND UNITED FUEL GAS COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Solicitor General, on behalf of the Federal Power Commission, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit, entered in the above-entitled case on August 2, 1961.

OPINIONS BELOW

The opinions of the Court of Appeals for the Fifth Circuit (App. A, *infra*, pp. 22-38) are reported at 293 F. 2d 761. The orders of the Federal Power Commission (R. 524-540, 585-591) are reported at 24 F.P.C. 204 and 525.

JURISDICTION

The judgment of the Court of Appeals setting aside the Commission's orders was entered on August 2, 1961 (App. C, *infra*, p. 44). A petition for rehearing, timely filed, was denied on October 5, 1961 (App. C, *infra*, p. 44). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTION PRESENTED

Respondent pipeline company filed increased rates predicated on a cost of service which included a claim to a 7 percent return on net investment. After suspension for five months, the new rates went into effect subject to refund of any portion not ultimately justified by the pipeline company. The Commission, treating separately the issue of rate of return, found, after full hearing, that 7 percent was excessive and that 6½ percent would be proper. It thereupon ordered a reduction, *pro tanto*, of the increased rates which were being collected subject to refund.

The question, which arises under Section 4 of the Natural Gas Act, is whether the Commission upon finding that a portion of the company's justification for the proposed rates is deficient may immediately order the rates reduced to the extent of the proved deficiency without awaiting the completion of all phases of the rate proceeding.

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717-717w, are set out in Appendix B, *infra*, pp. 39-43.

STATEMENT

The increased rate filing.—On October 5, 1959, Tennessee Gas Transmission Company tendered increased rates for filing pursuant to Section 4(d) of the Natural Gas Act, *infra*, p. 40. These rates represented an annual increase of \$26,590,138 in Tennessee's revenues based on sales for the test year ended July 31, 1959 (R. 503).¹ The need for this increase was predicated, *inter alia*, upon a claimed cost of service which included a return of 7 percent on investment (R. 498-501).

By order of November 4, 1959, the Commission set a hearing to determine the lawfulness of these new rates and suspended their operation for the statutory term of five months (R. 502-505). The hearing started on February 2, 1960 (R. 524).² On April 5,

¹ This increase was in addition to previous increases (FPC Docket Nos. G-11980 and G-17166) which are still pending before the Commission. Those increases had become effective, subject to refund, on July 14, 1957, and May 15, 1959, respectively, and totalled about \$24,077,000 and \$19,184,000 annually. Thus, the increased rates filed on October 5, 1959, were intended to produce about \$70,000,000 more in revenues than the rates last approved by the Commission.

² The Commission had originally ordered the hearing to commence on December 15, 1959 (R. 504), but by notice of November 16, 1959, granted Tennessee's request for a postponement.

1960, at the close of the five-month suspension period and during the course of the hearing, the rates became effective, subject to an undertaking by Tennessee to make refund of any portion found by the Commission not justified, together with interest thereon at the rate of 7 percent per annum (R. 505-509).

At the hearing, Tennessee presented all of its direct evidence. Its witnesses, however, were cross-examined only on the issue of rate of return. The staff of the Federal Power Commission and the West Virginia Public Service Commission presented evidence only on the rate of return, and their witnesses were cross-examined. None of the other interveners sought to present evidence on rate of return. Tennessee then presented rebuttal testimony on rate of return; cross-examination of this testimony was concluded on May 25, 1960 (R. 524-525).

After all the evidence on rate of return had been presented, the Commission staff counsel moved that the proceeding be divided into two phases: (1) determination of rate of return; (2) determination of the various other factors entering into the company's cost of service. He proposed further that, if it were found, in the first phase, that a proper rate of return was less than 7 percent, the Commission enter an interim order, reducing Tennessee's rates *pro tanto* and directing corresponding refunds for the past.²² Concurrently, staff counsel requested waiver of the examiner's intermediate decision on the issue of the rate of return (R. 525).

²² This proposal contemplated acceptance of all of Tennessee's other claims for purposes of an interim order.

Tennessee opposed this interim order procedure,³ relying upon the fact that the proper method of allocating Tennessee's cost of service among its six zones was contested, and that in another proceeding relating to Tennessee's rates for an earlier period (FPC Docket No. G-11980) the zone allocation issue had been tried and was awaiting decision by the hearing examiner (R. 591-606).⁴

On June 17, 1960, the Commission granted the motion to waive the intermediate decision on rate of return and provided for oral argument on that issue and on the question whether interim rate reductions and refunds should be ordered in the event Tennessee's 7 percent figure was found excessive (R. 513-516). Thereafter, on July 19, 1960, Tennessee filed an untimely⁵ motion requesting the Commission to waive the intermediate decision procedure with respect to the zone allocation issue in the other proceeding (No. G-11980) and to decide that issue simultaneously

³ Several interveners, including the so-called Columbia Companies (R. 607-625), also opposed this procedure. The related proposal of waiver of the examiner's decision on rate of return was unopposed (R. 513).

⁴ Tennessee also pointed out that the hearing examiner in No. G-11980 had ruled that determination of the zone allocation issue in that proceeding would govern the method of allocating costs among Tennessee's six zones in the instant case (R. 605).

⁵ The Commission's rules provide that motions requesting waiver of the examiner's intermediate decision shall be made no more than five days after conclusion of the hearings. 18 C.F.R. 1.30(c)(3). Hearings on the severed zone allocation issues in Tennessee's earlier case were concluded on December 17, 1959 (R. 522).

with the rate of return issue in this proceeding (R. 519-521). This motion, which was opposed by a number of parties (including the Columbia Companies), was denied on August 5, 1960 (R. 521-523).

On August 9, 1960, the Commission entered the order challenged below. It found that an overall rate of return of $6\frac{1}{8}$ percent was fair, just and reasonable for Tennessee. Accordingly, it disallowed Tennessee's rates, computed by the company on the basis of an excessive (7 percent) rate of return, and directed it to file interim reduced rates. It ordered that these interim rates become effective (subject to possible further refund at the conclusion of the entire rate proceeding) as of April 5, 1960, the date on which the disallowed rates had gone into effect, and that refunds be made to the extent that the company had collected, since April 5, 1960, amounts in excess of said interim rates (R. 524-540). The Commission pointed out that by requiring Tennessee to file substitute rates based on a proper rate of return, but otherwise based on the company's own claims, Tennessee and its customers would be placed in the same position as if Tennessee had originally filed increased rates based on a proper rate of return (R. 536).

On September 27, 1960, the Commission denied applications for rehearing filed by Tennessee and the Columbia Companies (R. 585-591). Both applications questioned the validity of the interim order procedure, and Tennessee also challenged the determination of the rate of return. The substitute rates, which have resulted in an annual revenue reduction

of about 10 $\frac{3}{4}$ million dollars, based on test year figures, have been in effect since November 1, 1960.⁶

Proceedings in the court below.—The court below unanimously affirmed the Commission's determination that a 6 $\frac{1}{8}$ percent rate of return was just and reasonable for Tennessee, but by a divided vote (Chief Judge Tuttle dissenting) set aside the Commission order to the extent that it required Tennessee to make lower rates effective immediately and to refund the amounts collected in excess of the substitute rates.⁷

On the latter issue, the majority concluded that, in the absence of a Commission decision on the zone cost-allocation issue, there was no basis for determining which of Tennessee's rates were unlawful; and that, although a natural gas company has the burden of justifying increased rates proposed by it, it "should not be held, at its peril, to the requirement of foretelling the decision of the Commission on the correctness" of such increased rates (App. A, *infra*, p. 33). The majority also stated that, regardless of the Commission's authority, the allocation of costs among zones is "such an essential element in determining whether the filed rates

⁶ Stays of the reduction and refund order were denied by the Fifth Circuit, Judge Wisdom dissenting. *Tennessee Gas Transmission Co. v. Federal Power Commission*, 283 F. 2d 729 (C.A. 5).

⁷ Chief Judge Tuttle wrote the court's opinion affirming the Commission's rate of return decision.

⁸ Tennessee has refunded \$7,416,663, plus interest, for the period from April 5, 1960 through October 31, 1960.

are excessive" that issuance of the interim rate order in advance of decision on the allocation issue was an abuse of discretion (App. A, *infra*, p. 34). Chief Judge Tuttle, dissenting, stated that he would have affirmed the Commission's order giving immediate effect to the conclusion that the rates based on an excessive rate of return were unreasonable. In his view, the applicant had the burden to establish each element upon which it predicated its rate increase, and Tennessee had no basis for complaint inasmuch as it was being relegated (by the Commission's interim order) to the precise position which it would have occupied had it based its rates, in the first instance, upon a proper rate of return (App. A, *infra*, p. 37). On October 5, 1961, the same panel of the court, Chief Judge Tuttle again dissenting, denied the Commission's petition for rehearing *en banc* (App. C, *infra*, p. 44).

REASONS FOR GRANTING THE WRIT

The decision below would prevent the Federal Power Commission from requiring an immediate reduction of a natural gas company's increased rates even though those rates are predicated in part upon an attempted company justification which had been found, after full hearing, to be deficient. It would prevent the Commission from continuing to use a procedure—interim rate orders—designed to carry out the mandate of Section 4 of the Natural Gas Act that the Commission decide increased rate questions "as speedily as possible" so as to relieve ultimate consumers of the burden of paying excessive

rates. We submit, moreover, that the decision below is inconsistent with the decisions of two other courts of appeals as well as with a ruling of this Court.

1. Under the Natural Gas Act, the seller initiates rate changes. See *United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division*, 358 U.S. 103; *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332. The rates, however, are subject to Commission review, and the Act expressly imposes upon the seller the burden of proving the justness and reasonableness of its increased rates. Section 4(e), *infra*, pp. 40-41. Here Tennessee filed increased rates for each of its six rate zones and attempted to justify them (and thus meet its burden of proof) on the basis of a cost of service which included a 7 percent return on its claimed net investment. This justification it failed to sustain. For, after a full hearing on the rate of return, the Commission found that 7 percent was excessive and that a rate of $6\frac{1}{8}$ percent was just and reasonable. In dollars and cents, this meant that the increased rates made and filed by Tennessee would have yielded revenues, on the basis of the test year, about eleven million dollars in excess of what Tennessee itself could properly justify when it made its filing, even if the remainder of Tennessee's case in support of these rates were accepted. Accordingly, the Commission disallowed the increased rates to the extent that they were predicated on this excessive rate of return and required Tennessee to file reduced rates reflecting a proper

return, but otherwise based on Tennessee's original presentation.*

Although the court below unanimously held that the Commission's determination of the rate of return was correct, the majority set aside that portion of the Commission's order which gave it immediate effect. The result is to permit the continued collection of company-made rates, which the company could not support when put to the test, from distributing company-customers and from ultimate consumers, who are, of course, intended to be the prime beneficiaries of regulation under the Natural Gas Act. See *Sunray Mid-Continent Oil Co. v. Federal Power Commission*, 364 U.S. 137, 147; *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 610.

The decision seems to rest largely on the erroneous view that consumers are fully protected, albeit they continue to pay excessive rates, by the pipeline's ultimate obligation to refund the excess charges with interest. But, as the Commission has recognized;¹⁰ the protection afforded by refund provisions is by no means complete. Ours is a mobile society; those consumers of natural gas who pay excessive rates in a given area today are scattered as the months go by. For the ordinary consumer, even if he does not move, a daily increase in his cost of living is not offset by

* Since the hearing had been concluded only with respect to the rate of return, Tennessee was permitted to put these new rates into effect, subject to refund, as of the date the disallowed rates had become effective (April 5, 1960).

¹⁰ See, e.g., Federal Power Commission Annual Report for 1953, p. 191.

the prospect of receiving a lump sum sometime in the future. Cf. *Brooklyn Savings Bank v. O'Neil*, 324 U.S. 697, 707-708. The Court has encountered this problem in the cases dealing with the disposition of funds impounded as a result of judicial stays of Commission rate reduction orders. See, e.g., *Federal Power Commission v. Interstate Natural Gas Co.*, 336 U.S. 577; *Central States Co. v. Muscatine*, 324 U.S. 138. Moreover, the inflationary impact of present-day high rates is scarcely relieved by the possibility of refunds at an indeterminate date in the future.¹¹

The pipelines' obligation to pay interest on refunds cannot be regarded as an effective deterrent to excessive rate filings. Quite the contrary. The vast amounts collected by the pipelines subject to refund, *infra*, p. 19, often provide a relatively cheap source of expansion capital. Although the pipelines make re-

¹¹ The structure of the Act gives apparent recognition to the imperfect nature of refund protection for the ultimate consumer. Otherwise, there would have been no need to grant the Commission power to suspend for a five-month period. It should be noted, in this connection, that the suspension provision of the Interstate Commerce Act, upon which the Natural Gas Act was modelled (see *Hope Natural Gas Co. v. Federal Power Commission*, 196 F. 2d 803 (C.A. 4)), was added because reparations were deemed an inadequate remedy for the shipper. See I Sharfman, *The Interstate Commerce Commission* (1931), pp. 201-202. It was also recognized that an unduly long suspension period would give inadequate protection to the carrier because of the inability to collect higher rates retroactively if it was later found that the carrier had been justified in filing its increased rates. Hence, provision was made to permit collection of increased rates, subject to refund, after the suspension period, imperfect as that protection might be. *Ibid.*

funds with 7 percent interest, the effective cost to them is much less. A corporation in the 52 percent tax bracket will recoup approximately half the cost of interest charges in tax deductions. Moreover, accretions to capital resulting from a continuing pattern of excessive charges increase a pipeline company's equity, which characteristically earns a substantially higher rate of return than its borrowed capital costs. Thus, the decision below takes from the Commission an effective tool for dealing with the prevalent practice of making consumers involuntary lenders.

2. *a.* The court below disapproved the interim order because the Commission had not heard and decided the cost allocation issue, although, for the purposes of this interim order, the Commission accepted Tennessee's allocation methods. This ruling runs counter to *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 583-585; *Panhandle Eastern Pipe Line Co. v. Federal Power Commission*, 236 F. 2d 606 (C.A. 3); and *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F. 2d 690, 715-716 (C.A. 8), certiorari denied, 346 U.S. 922.

In *Federal Power Commission v. Natural Gas Pipeline Co.*, *supra*, this Court affirmed an interim reduction of rates pursuant to a Section 5(a) investigation. It held, *inter alia*, that a company which had presented its entire direct testimony in support of its rates could not complain that it had not yet been able to examine Commission witnesses on aspects of the case which, for purposes of the interim order, the

Commission had decided on the basis of the company's presentation. 315 U.S. at 584.

In *Panhandle Eastern Pipe Line Co. v. Federal Power Commission*, *supra*, the Commission eliminated a portion of an increased rate after the company had presented its entire case in chief, disallowing about \$5,000,000 annually of Panhandle's proposed jurisdictional revenues. The Commission relied on its disallowance of the same elements in the preceding *Panhandle* case and pointed out that no new or supervening occurrences had been shown to warrant reconsideration of the Commission's recent decision. The Third Circuit, rejecting Panhandle's contention that no reduction could be ordered until all phases of the case had been resolved, held that a company which fails to make out a *prima facie* case in support of its cost of service is not entitled to continue collection of the unproved portion of its rates. The court pointedly observed (236 F. 2d at 608):

* * * Panhandle must have based its claim for a higher rate of return upon justification existing at the time of filing. It is difficult to see how else a change could have been proposed in good faith. True, in recognition of the time involved in these often long drawn out rate proceedings, the commission quite properly permits the basic showing of the justification which existed at the time of filing to be supplemented by evidence of occurrences since filing. But this is far from saying that a party who tries and fails to make a *prima facie* showing to support severable elements of his claim is entitled to a postponement of adjudication thereon in anticipation of possible new justifi-

cation which some future event may supply before the overall case can be completed.

Here the record shows that Panhandle was given full opportunity to offer all of its evidence in support of the items which the commission disallowed in the order now on appeal. Thereafter, the commission was under no obligation to postpone its ruling on those matters. * * * [12]

In the *State Corporation Commission* case, *supra*, the Eighth Circuit affirmed the Commission's interim reduction of increased rates filed by **Northern Natural Gas Company** to reflect the disallowance of \$7,601,853 of the company's claimed cost of service. As in the *Panhandle* case, the portion disallowed consisted of elements which the Commission had rejected in Northern's preceding rate case and as to which the Commission found, after presentation of Northern's affirmative case, that no intervening changes had been shown warranting different treatment.

b. The instant case stands on no different footing merely because there is an unresolved issue as to allocation of the company's total costs. In fact, allocation issues of various kinds were also undecided in the *State Corporation* and *Panhandle* cases when the Commission directed immediate rate reductions.¹³ In

¹² Compare the statement of the court below that "in filing rates a public utility should not be held, at its peril, to the requirement of foretelling the decision of the Commission on the correctness of the rates. * * *" (App. A, *infra*, p. 33).

¹³ See *State Corporation Commission of Kansas v. Federal Power Commission*, 206^o F. 2d 690, 712 (C.A. 8) and *Panhandle Eastern Pipe Line Co.*, 25 F.P.C. 787, 38 P.U.R. 3d 332, pending on review, C.A.D.C., No. 16583.

all events, it is invariably true that the "other issues" (there are, of course, many issues in the typical rate case) which remain whenever the interim order procedure is invoked might conceivably result in an offset, i.e., the rate proponent might be able to prove that, although some elements in the cost of service were overstated, others were underestimated." The

"Although there is a theoretical *possibility* that, as a result of the Commission's zone allocation decision (not yet rendered), Tennessee may not be able to earn the 6 $\frac{1}{8}$ percent return found proper during the period prior to that decision (see App. A, *infra*, pp. 32-33), there is no basis for the court's statement (App. A, *infra*, p. 34) that the effect of this determination "makes it highly unlikely, if not impossible" for Tennessee to earn that return.

In the first place, even the *possibility* can come to pass only if, after the allocation decision, Tennessee's rates in some zones are raised above the level of the substitute increased or interim rates now on file, while Tennessee is required to make full refunds in other zones. At the time the case was argued below, the presiding examiner had concluded in the related Tennessee case (No. G-11980) that Tennessee's allocation method should remain substantially unmodified. Although this, to be sure, was not a final decision, the court of appeals certainly had no reason to presume that a drastic change in zone allocations was forthcoming. Nor could it be presumed that the rest of Tennessee's claimed cost of service would be approved. Tennessee's interim rates, on a test year basis, are still \$59,000,000 in excess of any previously allowed Tennessee. Indeed, in the second phase of the rate proceeding before the Commission, which is now awaiting an examiner's decision, the Commission staff is advocating adoption of a total cost of service about \$36,000,000 less than that contended for by Tennessee.

In addition, we note that the Commission is not compelled to translate the results of allocation methods directly into rates, even prospectively, if it concludes that the impact will be detrimental to the public interest. See *Interstate Power Co. v. Federal Power Commission*, 236 F. 2d 372 (C.A. 8), certiorari denied, 352 U.S. 967.

crucial consideration is that under Section 4(e) the natural gas company has the burden of justifying its claimed increases. It cannot complain, therefore, if the Commission holds merely that it cannot continue to collect revenues which it has not justified on the basis of its own theory and evidentiary presentation.¹⁵

c. Nor can this case be distinguished on the ground that the examiner in the related Tennessee case (No. G-11980) had already heard evidence on the matter of zone allocation when the interim order was entered in this proceeding. Not all issues as to which evidence has been taken are susceptible of simultaneous decision. The complex zone allocation issue in No. G-11980 produced an evidentiary record of 4,500 pages and several score of exhibits. The interests of over ninety interveners were involved. The Commission was warranted in concluding that it should have the benefit of the examiner's determination of this issue.¹⁶ As events developed, the examiner's decision on this matter, covering some 131 pages of text, was not handed down until February 13, 1961 (more than six months after the interim order in the instant proceeding), and the matter has since been argued and

¹⁵ The majority below (App. A, *infra*, p. 34) erroneously assumes that the Commission, in finding that it would be proper for a company to earn a particular rate of return, guarantees that such a return will be earned. To the contrary, the Commission's conclusion as to the propriety of a particular rate of return means only that such a return was deemed proper on the basis of a test year and that rates designed to produce such a return in the future are permissible.

¹⁶ It is also pertinent that, while none of the parties had objected to waiver of the intermediate decision on rate of return, strong objection was made by a number of interveners to waiver of such decision with respect to the zone allocation issue.

reargued before the Commission.¹⁷ This chronology emphasizes that the Commission had good reason, in the interest of expedition, to put its rate of return determination promptly into effect. At the same time, there was little reason to believe, as we have shown (fn. 14, *supra*, p. 15), that Tennessee would ultimately suffer from the Commission's decision not to await the determination of the issue of allocation of costs.

3. The decision below has substantial importance both because of the broad thrust of the holding and because of its practical bearing upon the Commission's efforts to afford expeditious relief to consumers of natural gas.

To be sure, the majority opinion of the court of appeals emphasizes that this case involves an unresolved issue as to zone allocation.¹⁸ The decision, however, appears to have wide application. For one thing, allocation issues loom in the background of virtually every major pipeline rate case. Moreover, if cost allocation, as the majority has said (*infra*, p. 34), is "an essential element in determining whether the filed rates are excessive," it would seem that other elements which enter into the cost of service would similarly be deemed "essential." And, if this is so, the practical consequence is that the Commission may never order any reduction in rates—although in particular aspects the proponent has failed to make out its case—until it has disposed of all significant issues in a rate proceeding.

¹⁷ The reargument was held in September 1961 and the matter is now awaiting decision.

¹⁸ There are also other unresolved issues in Tennessee's case—issues upon which the examiner has not yet passed.

If public utility rate proceedings were run-of-the-mill cases, the matter would not be a grave one. But almost invariably such proceedings are complex and protracted, involving many parties and numerous difficult issues. Some of these issues, if severed, may be determined fairly promptly. It may be possible, for example, to decide an issue on the basis of a prior decision involving the same company, or, on the basis of a relatively brief presentation of expert testimony. Other issues, however, will characteristically require extensive study and investigation by lawyers, engineers and accountants even before any attempt be made to put in the relevant evidence. As a result, the final resolution of all issues presented by a full-blown rate case may take years, rather than months, even though every effort is made by the Commission to expedite the proceeding. Accordingly, the question whether the Commission may effectively decide one or more issues before it disposes of all of them becomes a matter of considerable practical moment.¹⁹ The decision below, in our view, threatens to destroy the utility of the interim rate procedure. Its significance as

¹⁹ In the *Panhandle* case, *supra*, the amount disallowed by the interim order constituted about 40%, on an annual basis, of the total disallowance ultimately ordered by the Commission in those proceedings, while in the *State Corporation Commission* case, *supra*, the interim reduction represented the full disallowance made. See *Northern Natural Gas Co.*, 13 F.P.C. 1518.

a precedent is heightened by the fact that many of the country's major pipelines have access to the Fifth Circuit.

Pipeline rate increases have become more and more frequent in recent years. Enormous amounts are now being collected subject to the possibility of ultimate refund. At the close of the fiscal year 1961, increased rate proceedings involving 41 pipeline companies were pending before the Commission. These companies were collecting, on an annual basis, approximately \$375,000,000 in increases not yet approved by the Commission. In the light of past experience, it must be assumed that a substantial portion of these increases will be found unjustified. Thus, during the fiscal year 1961, the Commission, concluding 31 cases involving increased rates by pipelines, disallowed approximately 37 percent of the increases for which those companies had filed. More than half of this disallowance (approximately 56 percent) resulted from a reduction of the amount claimed for return on net investment.²⁰

²⁰In the present case, the total amount of the proposed increased rates which will be disallowed by the Commission is not yet known. It is, therefore, impossible to state the percentage thereof represented by the interim order's disallowance of approximately \$11,000,000 (the amount of disallowance resulting from reduction in the rate of return). But the maximum is probably indicated by the Commission staff's contention that an additional \$36,000,000 should be disallowed. Even if the Commission disallowed everything contended for by its staff, the \$11,000,000 interim reduction would approximate 23% of the total disallowance.

The Commission believes that the interim order procedure, though certainly not a solution to all problems presented by a serious backlog of cases, is an important tool—one which will aid it in the strenuous effort which it is currently making to determine rate questions “as speedily as possible” (Section 4(e)) and to provide reasonably prompt relief from excessive charges.²¹ Indeed, within the space of the past several weeks the Commission staff has proposed the use of this procedure in two major pipeline cases.²² The instant case will determine in large measure whether this course is a fruitful one.

²¹ The Commission is mindful of the fact, noted on more than one occasion by this Court, that there have been inordinate delays.

²² *El Paso Natural Gas Co.*, F.P.C. Docket Nos. G-4769, et al., Tr. pp. 4063-4086 (Nov. 16, 1961); *Cities Service Gas Co.*, F.P.C. Docket No. RP 62-1, Tr. pp. 202-261 (Sept. 13, 1961).

In the *El Paso* case, the California Public Utilities Commission, the City of El Paso, and several California distributing companies, in addition to the Commission's staff, have requested use of the interim order procedure.

In the *Cities Service* case, the Commission staff's request for use of the interim order procedure was opposed by the customer companies, but principally because the pipeline had indicated that it would challenge the procedure in court on the basis of the decision below.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this petition for a writ of certiorari should be granted.

ARCHIBALD COX,

Solicitor General.

WILLIAM H. ORRICK, Jr.,

Assistant Attorney General.

MORTON HOLLANDER,

Attorney.

RALPH S. SPRITZER,

General Counsel,

HOWARD E. WAHRENBROCK,

Solicitor,

LUKE R. LAMB,

Assistant General Counsel,

PETER H. SCHIFF,

Attorney,

Federal Power Commission.

DECEMBER 1961.

APPENDIX A

In the United States Court of Appeals
For the Fifth Circuit

No. 18547

TENNESSEE GAS TRANSMISSION COMPANY, PETITIONER,

versus

FEDERAL POWER COMMISSION, RESPONDENT.

No. 18597

THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE
OHIO FUEL GAS COMPANY, AND UNITED FUEL GAS
COMPANY, PETITIONERS,

versus

FEDERAL POWER COMMISSION, RESPONDENT.

PETITIONS FOR REVIEW OF ORDERS OF THE FEDERAL POWER
COMMISSION.

(August 2, 1961)

Before TUTTLE, Chief Judge, CAMERON and
WISDOM, Circuit Judges.

TUTTLE, Chief Judge: These two petitions for review of orders of the Federal Power Commission attack, from somewhat different points, interim orders finding a $6\frac{1}{8}\%$ rate of return just and reasonable, and putting said rate of return into effect before resolving other issues touching on the allocation of

costs between different zones of operation of Tennessee Gas Transmission Company. Generally the name "Tennessee" will be used interchangeably with petitioner, and the name "Columbia Companies" will be reserved to discuss the petition of Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company.

The history of the proceedings leading up to the orders complained of is taken almost completely from the statement in petitioner's brief. In using such statement we have, however, eliminated some expressions of opinion and explanatory statements:

Tennessee owns and operates a natural gas pipeline system extending in a northeasterly direction from its sources of supply in Texas and Louisiana through the States of Texas, Louisiana, Arkansas, Mississippi, Alabama, Tennessee, Kentucky, West Virginia, Ohio, Pennsylvania, New Jersey, New York, Massachusetts, New Hampshire, Rhode Island and Connecticut. The rates charged by Tennessee for the transportation of natural gas and sales for resale of natural gas in interstate commerce are subject to the jurisdiction of the Commission under the Natural Gas Act (15 U.S.C. 717-717w).

On October 5, 1959, Tennessee filed with the Commission, pursuant to Section 4(d) of the Natural Gas Act, schedules of rate changes designed to recover the increased cost of providing natural gas service. These schedules set forth the respective rates proposed by Tennessee for each type of service in each rate zone on the Tennessee system. The Tennessee system is divided into six rate zones, with rates differing among the zones to give effect to distance, as well as other factors.

By order issued November 4, 1959, the Commission ordered a hearing to determine the "lawfulness" of the rates which had been filed. Following a five-month period of suspension, the rates became effective April 5, 1960, subject to an undertaking by Tennessee, required by Commission order, to "refund at such times and in such manner as may be required by final order of the Commission, the portion of the increased rates found by the Commission in this proceeding not justified, together with interest thereon at the rate of 7 percent per annum."

Hearings commenced on February 2, 1960, and continued intermittently until recessed on May 25, 1960. During the course of the hearings, Commission Staff Counsel moved that the hearing be divided into two phases. He proposed that the first phase deal solely with the issue of rate of return, and the remaining issues be reserved for a later stage of the proceeding. Staff Counsel further proposed that upon completion of the first phase of the proceeding, the Examiner's decision be omitted; that the Commission issue a decision determining the fair rate of return for Tennessee; and that the Commission issue an interim order requiring Tennessee to reduce its rates and make refunds, in the event the Commission concluded that the fair rate of return is less than claimed by Tennessee.

When Staff Counsel made his motion, there was pending before the Commission, in another proceeding involving Tennessee (Docket No. G-11980), an issue as to the proper method of allocating Tennessee's cost of service among its six rate zones and various services. By order issued April 30, 1959, in Docket No. G-11980, the Commission ruled that determination of the allocation issue should be expedited and, to that end, severed that issue for sepa-

rate and prior hearing and determination in that case. At the time Staff Counsel made his motion, the allocation issue had been thoroughly tried and briefed and was before the examiner for decision. Additionally, the Examiner in the instant proceeding had ruled that the determination of the allocation issue in Docket No. G-11980 would govern the method of allocating Tennessee's cost of service in this case.

Since it contended that determination of the allocation issue was required in order to translate the cost of service into rates for the various zones and services, Tennessee filed a memorandum opposing the Staff's motion for an interim order on the ground, *inter alia*, that such order would be illegal unless the Commission simultaneously determined the allocation issue. On July 19, 1960, Tennessee filed a motion with the Commission requesting it to determine the allocation issue simultaneously with the issue of rate of return. By order issued August 5, 1960, the Commission denied Tennessee's motion.

On August 9, 1960, the Commission issued its order, herein sought to be reviewed, adopting the Staff's interim order procedure. As stated above, by such order the Commission disallowed Tennessee's claim for a 7 percent return, fixed a $6\frac{1}{8}$ percent rate of return, required Tennessee to file reduced rates retroactively to April 5, 1960, and required Tennessee to make refunds for the differences in rates collected since April 5, 1960. The Commission's order did not, however, make any determination as to the proper method of cost allocation which should be employed in allocating the reduced cost of service among the six rate zones on the Tennessee system. Nor did the Commission make a determination as to which of the various rates filed

by Tennessee were unlawful, which rates should properly be reduced, or to whom refunds were lawfully due. Instead, the Commission left these questions open for later determination.

On August 29, 1960, Tennessee filed its application for rehearing which the Commission denied by its order issued September 27, 1960. On October 3, 1960, Tennessee filed its petition to review with this Court and simultaneously filed a motion for stay of the Commission's order. On October 28, 1960, this Court, with one Judge dissenting, denied the motion for stay.

Although Tennessee summarizes its extended specifications of error by placing them in five numbered paragraphs,¹ we discuss them under two headings:

(1) The rate of $6\frac{1}{8}$ percent was based on findings "unsupported by substantial evidence and is unreasonably low."

(2) The Commission erred in putting a rate less than 7 percent into effect by an interim order prior to determining whether the cost allocations between the six zones were lawful.

Considering first the $6\frac{1}{8}$ percent rate, we find that the Commission had before it a full record disclosing

¹This summary is as follows:

"1. The Commission erred in allowing Tennessee an over-all rate of return of only $6\frac{1}{8}$ percent. Such rate of return is confiscatory, deprives Tennessee of property without due process of law in contravention of the Fifth Amendment of the Constitution of the United States, and constitutes discriminatory, arbitrary and capricious action against Tennessee.

"2. The $6\frac{1}{8}$ percent rate of return is based on findings unsupported by substantial evidence and is unreasonably low in that:

a. It fails to yield a return on common book equity commensurate with returns being earned by enterprises having corresponding risks.

sufficient economic factors to permit it to determine what was a just and reasonable return. Both Tennessee and the Commission recognize that the standard and principles to be observed in testing the correctness of the Commission's findings are to be found in the two cases: *Bluefield Waterworks & Improvement Co. v. Public Service Commission of W. Virginia*, 262 U.S. 679, 692, and *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591.

The petitioner greatly stresses the following language from the Hope case:

"... the return to the equity owner should be commensurate with returns on investments in

b. It is unjustifiably less than the rate of return allowed by the Commission in its most recent decisions to pipeline companies having a more secure capital structure than Tennessee.

c. It fails to provide the margin of safety over the cost of debt necessary to prevent the quality of Tennessee's senior securities from deteriorating and being downgraded.

3. The Commission arbitrarily required Tennessee to reduce the rate of return on its natural gas production properties even though the Commission set for further hearing the issue of the rate of return to be allowed on such properties.

4. The Commission erred in the computation of Tennessee's capital structure in failing to include as common equity capital the convertible preferred stock which was in the process of being converted into common stock, and in failing to include in the capital structure mortgage bonds which had been issued by a Tennessee subsidiary.

5. The Commission illegally and arbitrarily set aside Tennessee's rates without deciding the cost allocation issue, which decision was necessary in order for the Commission to determine which, and to what extent, the individual zone rates filed by Tennessee were unlawful."

other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital. . . ."

Although the Commission does not counter by emphasizing any particular language of the opinion, we cannot overlook the following:

" . . . It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. The fact that the method employed to reach that result may contain infirmities is not then important. Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a presumption of validity. And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences. Cf. *Railroad Commission v. Cumberland Tel. & Tel. Co.*, 212 U.S. 414; *Lindheimer v. Illinois Bell Tel. Co.*, *supra*, pp. 164, 169; *Railroad Commission v. Pacific Gas & Electric Co.*, 302 U.S. 388, 401." 320 U.S. 591, 602.

In stressing the language, "The return to equity owners should be commensurate with returns on investments in other enterprises having corresponding risks," petitioner argues extensively from the tables showing *average earnings* of the ten major pipelines over an eight-year period ending with 1958 and for the 41 pipeline companies comprising the entire industry over a ten-year period ending in 1959. It also

strongly emphasizes the fact that the $6\frac{1}{8}$ percent return will yield the lowest return on common stock equity for any of its years of operation.²

The weakness of this approach is twofold: (1) There is no basis for Tennessee's implied assumption that it or any of the pipeline companies are entitled to the same return on book equity which they have historically enjoyed. "A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally." *Bluefield Waterworks & Improvement Co. v. Public Service Commission*, *supra*, p. 893. (2) The Commission found that petitioner was not an "average" pipeline company but rather that it is one of the largest and soundest. It is thus a non sequiter for petitioner to argue that because the eight or nine year average return on common equity of a group of companies has been higher than 10.12 percent then that rate is not just and reasonable for Tennessee for 1960.

The Commission specifically stated that it did "give consideration to the evidence of the return on book equity of Tennessee as compared to the other major pipeline companies as a factor in fixing a return which is commensurate with returns on investments of other enterprises having corresponding risks." With the evidence touching on the returns on book equity of other major pipeline companies present in the record, we cannot find, as invited to do by petitioner, that this statement of the Commission is without foundation.

² It is not disputed that the 7 percent overall return sought by Tennessee would have provided a 12.70 percent return on the book value of Tennessee's common equity capital or that the $6\frac{1}{8}$ percent overall return would provide a 10.12 percent return on common equity.

Petitioner strongly attacks the weight attributed by the Commission to the "earnings-price" ratios of Tennessee as bearing on its competition for the investor dollar. We think it clear that the Commission used such comparison to test the degree to which the investing public considered the return to be "commensurate" with other pipeline companies. Touching on this matter the Commission said, "Such data indicate that Tennessee enjoys a favorable and improving position in the money market in relation to the rest of the industry."

We have carefully analyzed the criticisms levelled by the petitioner on both the method used by it and its conclusions explaining its reason for adopting the $6\frac{1}{8}$ percent rate of return, and we find them to be without substance on the record before us. Moreover, we find no merit in the contention that the Commission erred, in the computation of Tennessee's capital structure, in failing to include as common equity capital the convertible preferred stock which was in the process of being converted into common stock and in failing to include in the capital structure mortgage bonds which had been issued by a Tennessee subsidiary. We consider the treatment given to these two items by the Commission as well within its discretionary powers.

We next come to the challenge of the Commission's applying the $6\frac{1}{8}$ percent rate of return to Tennessee's natural gas production properties before a determination was made as to whether a different rate of return was justified for these properties. The Commission answers this complaint in two ways. It says, first, that Tennessee did not distinguish, in its application for a 7 percent overall rate, between the rate of re-

turn it was entitled to receive on its production properties from the overall rate. We think this is not an adequate answer, because a larger return for production properties may well have been recovered under a 7 percent overall rate, whereas this might not be the case under a $6\frac{1}{8}$ percent overall rate if production properties were later found to be entitled to a higher rate of return. However, as to the second point urged by the Commission, we think it fully answers petitioner's contention. In allowing $6\frac{1}{8}$ percent rate of return, the Commission postponed for future consideration the treatment to be afforded substantial amounts received by petitioner through its treatment of federal income tax provisions for statutory depletion and intangible well-drilling costs. The Commission concluded that if Tennessee shows that it is entitled to a higher return on that part of its capital that is represented by production properties, this can be provided for when the Commission makes a final disposition of the treatment of the two tax benefits reserved for later consideration.

We next come to the complaint that the Commission could not legally enter the interim order denying the 7 percent rate of return and inviting the filing of new schedules based upon a $6\frac{1}{8}$ percent rate so long as there remained unresolved the question whether the allocations of cost among the six zones of operation would ultimately be approved by the Commission.

A majority of the Court, with the writer of this opinion dissenting, concludes that the Commission could not legally effectuate its order requiring the $6\frac{1}{8}$ percent rate of return to be given effect until it had made its determination as to the proper allocation of

cost of service among the several zones. The following part of the opinion, written by Judge Wisdom, and concurred in by Judge Cameron, becomes the Court's opinion touching on this phase of the appeal:

WISDOM, Circuit Judge: On April 30, 1959, in another proceeding involving Tennessee, in Docket No. G-11980, the Commission issued an order stating:

"It is our view that separate and prior hearing on the issues relating to the principles and methods to be applied toward allocation of costs among the zones on Tennessee's system and among the classes of service within the zones will aid in the disposition of this proceeding and may be of similar aid in disposition of proceedings in Docket No. G-17166."

The Examiner in this proceeding rules that the cost allocation as determined in Docket No. G-11980 would govern the allocation of service in this case. The cost allocation issue is ready for decision.

What the Commission in 1959 considered a reasonable and orderly sequence of proceedings seems equally reasonable and orderly now.¹

The Commission's refusal to decide the cost allocation issue means that there is no basis for determining which of the filed rates in specific zones are unlawful, the extent to which individual rates should be reduced, or to whom refunds are due. Meanwhile, the effect of the interim order is to continue the alleged discriminatory differential in favor of Zones 1, 5, and 6, although the Columbia companies, operating in Zones 2, 3, and 4, for several years have been endeavoring to have the Commission determine a proper

¹ In *Tennessee Gas Transmission Co.*, FPC Docket No. G-5259, the Commission issued an order holding that it would be "premature," "unfair" and "improper" to issue an interim order before determining pending allocation issues.

cost allocation among the zones. Tennessee will be injured, because it will not be able to recover adequate costs of services from the undercharged distributors in Zones 1, 5, and 6. For that matter, Tennessee would be injured if it were entitled to an overall return of 7 percent on its investment. It will be injured in any case because of the retroactive effect that will follow from the Commission's belated determination of cost allocation. This effect works in favor of Tennessee's overcharged customers, who are entitled to refunds, but works against Tennessee since it may not recoup from undercharged customers. Tennessee, therefore, will be unable to earn the return the Commission considers just and reasonable, no matter what that rate is.

It is true, of course, that the allocation of costs in all six schedules was made by Tennessee; that if these allocations are correct and are approved Tennessee will not be damaged; that the burden rests on the applicant to justify each rate increase. But conditions change, costs are not static, and rates are at best an educated guess. It seems that in filing rates a public utility should not be held, at its peril, to the requirement of foretelling the decision of the Commission on the correctness of the rates. The statute appears to have been designed on the assumption filed schedules will have to be adjusted. Lawful rates may be determined only after a full hearing; until the Commission fixes rates the utility is protected by being allowed to collect at the filed rate but under bond and subject to refund, and the consumer is protected by the refund of excess charges with 7 percent interest.

We question whether the hearing in which the cost allocation issues was excluded was the "full hearing" contemplated in Section 4 (e) of the Act. We ques-

tion whether the order, issued after a hearing in which the issue of cost allocation was barred, is a lawful order. It seems, too, that when the retroactive effect of the eventual determination of cost allocation makes it highly unlikely, if not impossible, for a utility to earn a "just and reasonable return," such an interim order lacks the weight and legal effect courts properly give to most orders of the Commission. Finally, regardless of the Commission's authority to issue the order, we hold that cost allocation among zones is such an essential element in determining whether the filed rates are excessive that it is unreasonable and an abuse of discretion to issue an interim rate order before deciding a pending allocation issue ripe for decision.

PER CURIAM:

The Court concludes that the manner in which the foregoing opinions can be given effect is to approve the order of the Commission as to all matters dealt with by it in the challenged order except its decision that the order was to become effective prior to a final determination of the allocation issue, and except the order requiring immediate refunds of the excessive rates collected under the suspended schedules. The order of the Commission is in these respects set aside. The case is remanded to the Commission for further proceedings not inconsistent with this opinion.

CAMERON, Circuit Judge, Concurs in the Result.

TUTTLE, Chief Judge, DISSENTING IN PART:

Although all members of the Court are in accord on the matters discussed in the main body of the opinion, I respectfully dissent from that part of

the opinion that holds that the reduced rate of return cannot be legally effectuated by a Commission order until the Commission makes the determination of allocation of cost of service.

The significance of this issue is made apparent by the petition of the Columbia Companies. This petition asserts that these companies have consistently opposed the schedules filed by Tennessee to be effective in zones 2, 3 and 4, in which they operated because, so they alleged, Tennessee had allocated its cost of service unfairly against their interests and in favor of zones 1, 5 and 6. It is asserted that by reducing the rate to be charged by cutting from 7 percent to $6\frac{1}{8}$ percent the rate of return, this would increase the amount by which zones 1, 5 and 6 are underpaying their proper rates. It is clear that if the Commission should later determine that cost allocations improperly favored zones 1, 5 and 6, the customers in those zones would be benefitted to the extent that they had obtained the gas at the rate now approved by the Commission's interim order. This follows from the structure of the statute which makes rate increases prospective only. In other words, there is no way in which Tennessee could hereafter, if we approve this $6\frac{1}{8}$ percent order, collect additional sums to make up for the advantage zones 1, 5 and 6 will have enjoyed because they were favored temporarily with a cost of service allocation improperly weighted in their favor.

Columbia's next contention, however, does not follow from this fact. Columbia claims to be prejudiced because it says zones 1, 5 and 6 may subsequently be found to have received gas too cheaply at Columbia's expense. It is true that it is possible that the Commission may find that zones 1, 5 and 6 have received gas too cheaply. The weak-

ness of Columbia's position, however, is that Columbia is not, and cannot be, hurt by any such subsequent determination. This follows because the rates which Columbia is now paying are still being paid subject to a final determination as to their lawfulness *as to all matters except* the rate of returns on the common equity. Thus, it will be entitled to a refund of all amounts it may be found to have paid in excess of the correct rate because of an improper allocation of costs of service. Columbia is now immediately benefitted to the extent that it is paying, subject to refund, on schedules including a $6\frac{1}{8}$ percent rather than a 7 percent rate of return. It is not an aggrieved party merely because the Commission did not proceed to a final determination of other possible savings to it at the same time.

The Columbia companies strongly argue that they are entitled under the statute, as an interested party, to a determination by the Commission of their complaint of undue preferences granted to the other zones in violation of Section 4(b) of the Natural Gas Act. They are undoubtedly entitled to such a determination, but not necessarily before the Commission can eliminate what it finds to be an unlawful increment in the price structure. See *State Corporation Com. of Kansas v. F.P.C.*, 8 Cir., 206 F. 2d 690, cert. den. 3 U.S. 922. Columbia could be hurt in these circumstances only if Tennessee were to be permitted to withhold refunds to which Columbia might become entitled on the ground that it could not recoup from zones 1, 5 and 6, and therefore, it could not be required to refund excessive charges from zones 2, 3 and 4. As I will next show, this is *not* the law.

Tennessee claims that there is nothing in the Natural Gas Act that warrants the entry of an

order that has the effect of reducing the charges it can make until the Commission decides whether it may not be charging too little from three zones even though it may be charging too much in three others.

The Commission answers this in two ways: (1) the allocation of costs in all six schedules was made by Tennessee. If these allocations are correct and are approved Tennessee will not be damaged. If they are incorrect they will be corrected and Tennessee will be required to make additional refunds to customers in those zones that were unfairly burdened by the improper allocations, but it will be unable to collect for any increased rates as such that a correct allocation would have warranted from the customers in the zones where there was an unfairly low increment of cost of service. This, the Commission says, is only the natural result of the regulatory scheme envisaged by the Natural Gas Act. The burden rests on the applicant to justify each rate increase. This includes the burden to establish the correctness of the allocation of costs of service as to each schedule filed. Tennessee stands in no different position than if the Commission, after the section 4 hearing, decided that Tennessee was entitled to an overall return of 7 percent on its investment, just as asked for by Tennessee, but decided that the cost allocations between the several zones were discriminatory, as here claimed by Columbia. The Commission would not have the authority to *increase* the schedules filed by Tennessee in zones 1, 5 and 6, but it would be under the obligation to reduce those for 2, 3 and 4 and make refunds for excess amounts paid by Columbia. See *Interstate Power Co. v. Federal Power Com.*, 8 Cir., 236 F. 2d 372. In such a situation Tennessee would not realize the full permitted rate of return because it would have failed to substantiate the correctness of the cost allocation. Of

course, the Commission could, and should under such circumstances, authorize the filing of new schedules to have prospective effect to remedy the allocation imbalance, but it would have no power to authorize Tennessee to collect more from zones 1, 5 and 6 than its filed schedules called for. (2) The Commission has a second answer to Tennessee's criticism in this regard. It seems to say that Tennessee still has several unresolved rate increases pending, all of which affect these same zones, and, if Tennessee is found to have undercharged zones 1, 5 and 6, it may have ample funds collected under bond subject to refund to customers in these zones from which it can recoup for a failure to charge the permissible rate for the period of this present rate proceeding. I think we need not speculate on this matter because I think the first contention elaborated above is sound.

I would affirm the Commission's order in full.

APPENDIX B.

The Natural Gas Act of 1938, 52 Stat. 821, as amended, 15 U.S.C. 717, *et seq.*, provides, in pertinent part, as follows:

SEC. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate

to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the

sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract af-

feeting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

SEC. 16. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this act. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this act; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirement for different classes of persons

or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours.

SEC. 19. (b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28, United States Code. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. * * *

APPENDIX C

United States Court of Appeals

For the Fifth Circuit

OCTOBER TERM, 1960

No. 18,547

TENNESSEE GAS TRANSMISSION COMPANY, PETITIONER,

versus

FEDERAL POWER COMMISSION, RESPONDENT.

No. 18,597

**THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE
OHIO FUEL GAS COMPANY, AND UNITED FUEL GAS
COMPANY, PETITIONERS,**

versus

FEDERAL POWER COMMISSION, RESPONDENT.

**PETITIONS FOR REVIEW OF ORDERS OF THE FEDERAL POWER
COMMISSION.**

**Before TUTTLE, Chief Judge, CAMERON and WISDOM,
Circuit Judges.**

JUDGMENT

These causes came on to be heard on the petitions of Tennessee Gas Transmission Company and The Manufacturers Light and Heat Co., The Ohio Fuel Gas Company, and United Fuel Gas Company, for review of orders of the Federal Power Commission issued on August 9, 1960 and September 27, 1960 in Docket No. G-19983, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered, adjudged and decreed by this Court that the orders of the Commission in these causes be, and the same are hereby, approved in part and set aside in part in accordance with the opinion of this Court; and that these causes be, and they are hereby, remanded to the Commission for further proceedings not inconsistent with the opinion of this Court.

"CAMERON, Circuit Judge, concurs in the result."

"TUTTLE, Chief Judge, dissents in part."

Issued: August 2, 1961.

FILED

5th day of October 1961

CLAIR R. JAMES

Clerk of the United States Court of Appeals

In the United States Court of Appeals

For the Fifth Circuit

No. 18,547

TENNESSEE GAS TRANSMISSION COMPANY, PETITIONER,

v.

FEDERAL POWER COMMISSION, RESPONDENT.

No. 18,597

THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE
OHIO FUEL GAS COMPANY, AND UNITED FUEL GAS
COMPANY, PETITIONERS,

v.

FEDERAL POWER COMMISSION, RESPONDENT.

*Petitions for Review of Orders of the Federal Power
Commission*

(October 5, 1961)

ON PETITION FOR REHEARING

Before TUTTLE, Chief Judge, CAMERON and WISDOM,
Circuit Judges.

PER CURIAM:

It is ORDERED that the petition for rehearing filed in the above styled and numbered cause be, and the same is, hereby DENIED.

TUTTLE, Ch. J., Dissenting.

LIBRARY
SUPREME COURT. U. S.

Office-Supreme Court, U.S.
FILED

DEC 11 1961

JOHN F. DAVIS, CLERK

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1961

No.

105 50

CITY OF PITTSBURGH, PENNSYLVANIA,
Petitioner,

**TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT AND HEAT
COMPANY, THE OHIO FUEL GAS COM-
PANY, AND UNITED FUEL GAS COMPANY,**
Respondents

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE
FIFTH CIRCUIT**

DAVID W. CRAIG,
*City Solicitor, —
City of Pittsburgh,
Pennsylvania.*

**CHARLES S. RHYNE,
HERZEL H. E. PLAINE,**
*Rhyme & Rhyme,
400 Hill Building,
Washington, D.C.*

*Attorneys for Petitioner,
City of Pittsburgh,
Pennsylvania.*

INDEX

	Page
Opinions Below	3
Jurisdiction	3
Question Presented	3
Statute Involved	3
Statement	3
Pittsburgh's Relation to the Controversy	3
The Proceedings Before the Commission	4
The Proceedings in the Fifth Circuit	5
Reasons For Granting The Writ	9
1. The Importance of the Interim Order Procedure	9
2. The Authority of the Commission To Use The Procedure, and the Judicial Support For It	12
3. The Inadequacy of Refunds	15
Conclusion	17

TABLE OF AUTHORITIES

Cases:	
<i>Federal Power Commission v. Hope Natural Gas Company</i> , 320 U.S. 591	9
<i>Federal Power Commission v. Natural Gas Pipeline Company</i> , 315 U.S. 575	9, 14
<i>Gas Service Company v. Federal Power Commission</i> , 282 F. 2d 496 (DC Cir.)	16
<i>Mississippi Valley Gas Company v. Federal Power Commission</i> , 18501, Sept. 12, 1961 (F. 2d —, 65 Cir., No. 18501)	16, 17
<i>Pacific Natural Gas Company v. Federal Power Commission</i> , 276 F. 2d 350 (9 Cir.)	16
<i>Pinkshole Eastern Pipeline Company v. Federal Power Commission</i> , 236 F. 2d 606 (3 Cir.)	15
<i>State Corporation Commission of Kansas v. Federal Power Commission</i> , 206 F. 2d 630 (8 Cir.), cert. den. 346 U.S. 922	15

	Page
<i>Tennessee Gas Transmission Company v. Federal Power Commission</i> , 283 F. 2d 729 (5 Cir.)	7
<i>United Gas Pipeline Company v. Memphis Light, Gas and Water Division</i> , 358 U.S. 103	10, 16
<i>United Gas Pipeline Company v. Mobile Gas Service Corporation</i> , 350 U.S. 332	10
Statutes:	
Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821-833, as amended, 15 USC 717-717w:	
Section 4, 15 USC 717c	3, 4
Section 4(e), 15 U.S.C. 717c(e)	11, 12
Section 5(a), 15 USC 717d(a)	3, 14
Section 16, 15 USC 717o	3, 12
Section 19(b), 15 USC 717r(b)	2, 3
Miscellaneous:	
Federal Power Commission Annual Report, 1953, p. 101	16
Federal Power Commission Annual Report, 1960, p. 2	12
Federal Power Commission Orders:	
18 FPC 428	5
24 FPC 204, 525	2
Federal Power Commission Docket No. RP 62-1, re Cities Service Gas Company	17

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1961

No.

CITY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT AND HEAT
COMPANY, THE OHIO FUEL GAS COM-
PANY, AND UNITED FUEL GAS COMPANY,

Respondents

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE
FIFTH CIRCUIT**

Petitioner, the City of Pittsburgh, Pennsylvania (Pittsburgh) prays that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Fifth Circuit, entered in the above entitled cause on August 2, 1961, rehearing denied October 5, 1961. A similar petition for a writ of certiorari has been contemporaneously filed by the Solicitor General of the United States on behalf of the Federal Power Commission (Commission).

OPINIONS BELOW

The opinions of the Court of Appeals for the Fifth Circuit are reported at 293 F. 2d 761,¹ and printed as Appendix A of the petition for certiorari filed in this cause on behalf of the Federal Power Commission (at pp. 22-38 thereof). The orders of the Federal Power Commission (R. 524-540, 585-591) are reported at 24 FPC 204 and 525.²

JURISDICTION

The judgment of the Court of Appeals setting aside the Federal Power Commission's orders was entered on August 2, 1961. A timely petition for rehearing, filed by the Commission, was denied on October 5, 1961. The judgment, and order denying rehearing, are printed as Appendix C of the petition for certiorari filed in this cause on behalf of the Federal Power Commission (at pp. 44-46 thereof). The jurisdiction of this Court is invoked under the provisions of 28 USC 1254 (1) and Section 19(b) of the Natural Gas Act, 15 USC 717r(b).

QUESTION PRESENTED

The Commission has made a separate and complete determination, after full hearing, of a proper rate of return on net investment of an interstate transmission company in a rate increase proceeding under

¹ Covering Cases No. 18547 and No. 18597 in that Court. Pittsburgh was an intervening party, on the side of the Commission, in those cases, admitted by order of the Court October 19, 1960.

² Relating to FPC Docket No. G-19983. Pittsburgh has been and is an intervener in the proceedings before the Commission, admitted by order of the Commission April 28, 1960.

Section 4 of the Natural Gas Act. The Commission has found that the company, in filing and making effective new rates, was not justified in using a 7% rate of return in its cost of service, and fixed 6 $\frac{1}{8}$ % as the proper rate of return.

The question is whether, before it has disposed of other or all issues in the rate proceeding, the Commission may provide immediate relief to ratepayers from the charges established as excess by requiring the interstate transmission company to refile and reduce its increased rates by the amount of the known unjustified excess.

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act, Act of June 21, 1938, c. 556, 52 Stat. 821-833 as amended 15 USC 717-717w, namely, Sections 4, 5a, 16 and 19(b), are set out in Appendix B of the petition for certiorari filed in this cause on behalf of the Federal Power Commission (at pp. 39-43 thereof).

STATEMENT

Pittsburgh's Relation to the Controversy

Pittsburgh comprises about 700,000 inhabitants, most of whom are consumers of natural gas. Tennessee Gas Transmission Company (Tennessee) is an interstate transmission or pipeline company which sells large quantities of natural gas to distributor companies, including The Manufacturers Light and Heat Company (one of the respondent Columbia Companies), The Peoples Natural Gas Company, and Equitable Gas Company, who resell to Pittsburgh and its inhabitants as consumers.

Pittsburgh has been an intervener, representing its inhabitant consumers, in the rate increase proceedings before the Commission (admitted by Commission order April 28, 1960), and before the Fifth Circuit Court of Appeals (admitted by Court order October 19, 1960), because the increased rates charged by Tennessee to the distributors have been passed on to and are being paid by the consumers under tariff schedules of the distributors effective in Pennsylvania. For like reasons, the Pittsburgh consumers would be beneficiaries of the Commission's so-called interim order of August 9, 1960, which, if left undisturbed, would mean immediately effective lower rates (commencing November 1, 1960) and refunds of preceding excess charges to the consumers (from April 5, 1960 to November 1, 1960).

The Proceedings Before The Commission

The increased rate filing by Tennessee, out of which this controversy flows (identified before the Commission as Docket No. G-19983), is the third in a series of pending, contested and undisposed of annual increases in rates filed by Tennessee. In 1957, Tennessee filed an approximate \$24 million annual rate increase (Docket No. G-11980), in 1958 an approximate \$20 million annual rate increase (Docket No. G-17166) and in 1959 an approximate \$26 million annual rate increase (Docket No. G-19983). Under Section 4 of the Natural Gas Act, each of these increases was suspended by Commission action for the statutory 5 month period and then went into effect, and have been collected as filed, subject to refund, pending determination of their justness and reasonableness by the Commission. Together, the increases represented

a pyramiding of approximately \$70 million annually in increased rates.³

Hearings have been held in the first docket, No. G-11980, but the case was not complete when hearings began in the third docket, No. G-19983, and the first docket has not yet been determined by the Commission. No hearings have been held in the second docket No. G-17166.

In the third docket, No. G-19983, hearings commenced February 2, 1960 (1-524). Tennessee presented all of its direct case, but its witnesses were cross-examined only on the issue of rate of return. The FPC staff and one intervener presented evidence on the rate of return only and their witnesses were cross-examined. Tennessee presented rebuttal testimony on rate of return, and cross-examination of this testimony was completed May 25, 1960 (R. 524-525).

When the taking of evidence on rate of return had been concluded, FPC staff counsel moved that the proceeding be divided into two parts:

(1) Determination of the rate of return by the Commission directly, with omission of the hearing examiner's intermediate decision. He further proposed that

³ The Commission's disputed order of August 9, 1960, in Docket No. G-19983, which directed the refiling to conform with the proper rate of return, if permitted to stand, has the effect of reducing the \$70 million overall annual increase by about \$10³/₄ million annually from November 1, 1960, onward.

⁴ In this docket, the rates were predicated on a cost of service which included a 7% rate of return. The rate of return for Tennessee last approved by the Commission before then had been 6% in 1957, 48 FPC 428. In the two pending dockets preceding No. G-19983, the rates of return used by the company were less than 7% but more than the 6¹/₂% which the Commission later found to be reasonable in Docket No. G-19983.

if a proper rate of return was less than 7% the Commission should enter an interim order reducing Tennessee's rates to the extent of the reduced amount and directing corresponding refunds for the past, but using all else of Tennessee's presentation as presented by Tennessee (R. 377-378).

(2) Determination of the other elements entering into the company's cost of service following the usual procedure (which would include the presiding examiner's intermediate decision) (R. 525).

While omission of the examiner's decision on rate of return was unopposed (R. 513), Tennessee and the interveners described as the Columbia Companies (who are respondents here) opposed the interim order procedure (R. 591-606, 607-625). Tennessee relied upon the fact that the proper method of allocating Tennessee's cost of service among its six zones was contested, and that in the pending first rate increase docket for an earlier period of time, No. G-11980, the zone allocation issue (the determination of which the examiner had said would be similarly applied in the current docket) had been tried and was awaiting decision by the hearing examiner.

On June 17, 1960, the Commission granted the motion to omit an intermediate decision of the examiner on the rate of return, and provided for oral argument on the merits of the rate of return and on the procedure of ordering interim rate reductions and refunds if 7% was found excessive (R. 513-516). On June 19, 1960, by motion, Tennessee requested the Commission to waive the intermediate decision procedure on the zone allocation issue in Docket No. G-11980 and to decide that issue simultaneously with the rate of return issue.

in this proceeding, No. G-19983 (R. 519-520). The Commission denied this motion on August 5, 1960 (R. 521-523).

On August 9, 1960, the Commission entered the order disputed below, which determined that an overall rate of return of 6¹/₈% was fair, just, and reasonable for Tennessee. The order disallowed the rates computed at 7%, directed Tennessee to file interim reduced rates (subject to possible further refund at the end of the entire case) effective April 5, 1960, when the originally filed rates went into effect, and ordered Tennessee to make refunds from that date for any sums collected in excess of the interim reduced rates (R. 524-540). The Commission stated that in requiring Tennessee to substitute rates founded on a proper rate of return but otherwise using the company's own claims, Tennessee and its customers were put in the same position as if Tennessee had originally filed increased rates on a proper rate of return.

The Commission denied applications for rehearing by Tennessee and the Columbia companies, on September 27, 1960 (R. 585-591). Both applications attacked the interim order procedure, and Tennessee challenged the decision on the 6¹/₈% rate of return. The Commission pointed out that the order of August 9th providing for the filing of lower rates based on the 6¹/₈% return would result in a savings to Tennessee's jurisdictional customers of about \$11 million annually. The substitute filing, made in November 1960, has resulted in an annual revenue reduction, in relation to test year figures, of about \$10³/₄ million.⁶

⁶ Stays of the reduction and refund order were denied by the Fifth Circuit, Judge Wisdom dissenting. *Tennessee Gas Transmission Co. v. Federal Power Commission*, 283 F. 2d 729 (5 Cir.).

The Proceedings in the Fifth Circuit

The Court below unanimously affirmed the Commission's determination that 6 1/8% was a just and reasonable rate of return for Tennessee.

On the interim order procedure, however, by a 2 to 1 vote, Chief Judge Tuttle dissenting, the Court set aside the Commission order to the extent that it required Tennessee to make immediate refunds⁶ and to make lower rates effective immediately. The majority view was that the lack of a Commission decision on cost-allocation by zones meant there was no basis for determining which of the filed rates in specific zones were lawful; that while the allocation of costs in all the schedules was made by Tennessee and the burden rests on it to justify each rate increase, the company should not be held at its peril to foretell the decision of the Commission on the correctness of the increased rates; that, until the Commission fixes the rates, the company is protected by being allowed to collect at the filed rate and the consumer is protected by the company's obligation to refund any excess charges with interest; and finally, regardless of the Commission's authority to issue the order, the cost-allocation among zones is such an essential element in determining whether filed rates are excessive that it was an abuse of discretion to issue an interim rate order before deciding the allocation issue.

Chief Judge Tuttle, dissenting, would have affirmed the Commission's order giving immediate effect to the conclusion that the rates based on the excessive rate of return were unreasonable. In his view, under the

⁶ Tennessee has refunded over \$7 1/2 million for the period April 5, 1960 through October 31, 1960.

Natural Gas Act, Tennessee has the burden of establishing the validity of each element in its rate increase filing, including the cost allocations which it makes; and Tennessee cannot complain if it is placed, by the Commission's order, in the position it would have occupied initially had it based its rates on a proper rate of return.

On October 5, 1961, the same panel of the Court, Chief Judge Tuttle again dissenting, denied the Commission's petition for rehearing *en banc*.

REASONS FOR GRANTING THE WRIT

The decision below has impaired the continued ability of the Federal Power Commission to use an important procedural device for curbing, at least in part, unwarranted rate increases and collections of excess rates by interstate natural gas companies from customer purchasers and consumers of natural gas. The Fifth Circuit decision is in conflict with decisions of the Third and Eighth Circuits, and inconsistent with the views of this Court in *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U.S. 575, 583-585.

1. The Importance of the Interim Order Procedure. In keeping with the primary purpose of the Natural Gas Act "to protect the consumer interests against exploitation at the hands of private natural gas companies" (*Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 612), the interim order procedure may serve both as a direct remedy for consumers and as a deterrent to the interstate pipeline companies in the overstating of rate claims and the collection of unwarranted increases. The very existence (and validity) of the interim order procedure

as a potential remedy, even if put to use only infrequently, is most important to discourage the filing of exaggerated claims and rates based thereon. As used, and if upheld, in this case, it demonstrates that the Commission need not and will not stand by during the pendency of lengthy rate increase cases and permit the unjustified collection of huge sums in excess rates from customers and consumers, where some of the issues upon which the increases rest are subject to early separable examination and the justification is found to be deficient.

In this connection, the operative considerations which tend to foster the exaggerated claims and rate filings are that:

* (1) In the first instance, the interstate pipeline companies are in a position to put rate increases into effect without any dollar limitation or other measurable criterion (*United Gas Pipe Line Company v. Memphis Light, Gas and Water Division*, 358 U.S. 103; *United Gas Pipe Line Company v. Mobile Gas Service Corporation*, 350 U.S. 332).

(2) The usual pipeline rate increase case (encompassing Commission investigation and review by hearing) involves many issues and parties and often takes years for final disposition.

(3) Multiple rate increases may be filed by the same company and made effective before its first increase has been passed upon by the Commission. The respondent pipeline company, Tennessee, affords a good illustration of both this and the previous point, with three unresolved but effective increases filed in 1957, 1958, and 1959, respectively.

(4) The obligation of the pipeline company to ultimately refund with interest any sums found excess

is not a deterrent to unreasonable increases, apparently because of the huge store of capital involuntarily provided by the ratepayers at a worth exceeding the actual cost to the company. Treated as equity capital, these funds earn a much higher rate of return than their cost, for while the company makes refunds with 7% interest, it recoups a large part of the interest (about half, if the company is in the 52% tax bracket) as an income tax deduction. On the other hand, as noted hereinafter, the ultimate refund is not an adequate recompense to the ultimate ratepayer in contrast to the initial payment of lower rates; and industrial consumers, as distinct from other consumers, derive no refund protection from the suspension provisions of the Natural Gas Act (Section 4(e)).

That there is nothing mythical about the piling up of overstated rate increases is shown by some few statistics furnished by the Commission in its petition for certiorari (p. 19). At the end of fiscal year 1961, 41 pipeline companies were involved in pending rate increase proceedings. On an annual basis, the companies were collecting about \$375 million in unapproved increases. From past experience (using the 31 pipeline rate cases concluded in fiscal 1961 as an example) it would appear that a substantial portion of the total increases will be found unjustified (for fiscal 1961, the portion was 37%). More than half of the total disallowances in fiscal 1961 (about 56%) came from reduction of the claimed rates of return on net investment (the area covered by the interim order in this case):

In the case of the respondent Tennessee, of the total \$70 million annual increase effectuated by its three pending rate increase filings, the Commission has

already disallowed an estimated \$10³ million annually in current rates (about 23%) by reducing one item, the claimed rate of return in the third docket, and it appears that the FPC staff contends that an additional \$36 million should be disallowed.

2. The Authority of the Commission to Use The Procedure, and The Judicial Support For It. Opposed to the enumerated considerations which tempt, and tend to foster, the filing of excessive rate increases, is the obligation of the interstate natural gas company to justify to the Federal Power Commission the justness and reasonableness of the increased rate (Section 4(e), Natural Gas Act). Unfortunately for the consumer, this burden of proof is usually put to the test long after the increases have been effectuated, rather than earlier. Hence, in keeping with the express duty on the Commission (also imposed by Section 4(e)) to decide increased rate questions as speedily as possible, the basic Commission duty under the Act to protect consumers from the burden of paying excessive rates, and the broad rulemaking and ordering powers (Section 16), it would certainly appear that the Commission may adopt procedures to quicken the pace of proof, justification, and correction, including the early separate treatment of issues which lend themselves to such handling.

The rate of return issue decided in this case is an outstanding example of a separable issue which can receive early treatment. In contrast to other types of issues, rate of return requires no extensive field investigation by the Commission staff (see FPC Annual Report 1960, p. 2), and it presents a repetitive broad judgment question with which the Commission is quite familiar without being materially aided by a

hearing examiner's decision. On the other hand, the allocation issue discussed by the Court below, and certain other issues, appear to present problems in novelty and investigation which not only take longer to develop, but are of a nature that the Commission's consideration of them is enhanced by a hearing examiner's decision.

The obstacle to this separation, and separate corrective action, was expressed in the view of two of the three judges who sat below, that a later determination of the allocation issue might affect the earnings expected on the rate of return in each of the six zones used by Tennessee, particularly if the Commission approved an allocation formula different from that used by Tennessee; hence it was unreasonable to compel Tennessee to make a pro tanto correction of its rates before the allocation issue was decided.

The majority below appears to have overlooked the fact that in deciding on the reasonableness of one severable item of the cost of service, to wit, the proper rate of return, the regulatory agency does not guarantee to the company that such a return will be earned, overall or by zones. On the contrary, the regulatory agency has held only that the rate of return it fixed is proper on the basis of a test year, and that rates which will produce that return in the future are permissible, collectible rates. All else of the company's presentation and claims remains, for the present, undisturbed.

The view of the majority below fails to give appropriate weight to both the initial rate making capacity of the pipeline company, and the ultimate burden of proof on it. Tennessee, in keeping with

the concept of the statute, put together the various components constituting a cost of service upon which it based its increased rates, put the rates into effect, and then urged justification in the hearings before the Commission.

In terms of making the temporary or interim correction, the Commission has accepted each element of Tennessee's cost of service as presented by Tennessee, including the zone allocations devised by Tennessee, except the element of rate of return, which has been fully explored and modified to 6½% (the latter result affirmed by the Court of Appeals). The pipeline company cannot complain if all of its presentation continues to be given effect in rates except the one element which the company could not justify and which has been properly revised downward.

The view of the Fifth Circuit is not consonant with the views of this Court expressed in *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U.S. 575, 583-585, where this Court upheld an interim order (in a Section 5(a) rate investigation) reducing rates. The Court recognized as appropriate the two step procedure of first "adjustment of the general revenue level to the demands of a fair return", and second, "adjustment of a rate schedule conforming to that level so as to eliminate discriminations and unfairness from its details." In sustaining the interim order, the Court held that the companies were not hurt because the Commission had entered the order on the basis only of the companies' presentation of testimony, without cross-examination of such testimony or testimony by Commission witnesses, 315 U.S. at 584 (a situation much less complete than the instant case where the entire testimony and cross-examination was

submitted on both sides of the issue covered by the interim order).

In *Panhandle Eastern Pipeline Company v. Federal Power Commission*, 236 F. 2d 606 (3 Cir.), the Third Circuit rejected the company's claim that no reduction of a rate increase could be ordered until all phases of the case had been resolved. The Court held that the company had been given the opportunity to offer all of its evidence in support of the severable elements of its claim, and had, in the view of the Commission, failed to make a prima facie showing in support thereof; therefore the Commission was under no obligation to postpone its disallowance of the items (providing a rate reduction of about \$5 million annually).

In *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F. 2d 690, 715-716 (8 Cir.), cert. denied 346 U.S. 922, the Eighth Circuit affirmed an interim reduction of approximately \$7½ million in increased rates filed by Northern Natural Gas Company, comprising elements as to which the Commission was of the view that the company had not made out a case.

In both of these cases there remained other issues, including allocation matters, to be disposed of by the Commission, but the rationale of the holdings is that the natural gas companies cannot continue to rely, and collect rates predicated, upon elements in the cost of service which have been found by the Commission to be overstated and unjustified.

3. The Inadequacy Of Refunds. The Court below appears to have assumed that the consumers, who continue to pay the excessive rates, are amply protected by the obligation of the pipeline to refund the excess

charges with interest. Unfortunately, for the ordinary householder, in contrast to the initial payment of lower rates and holding the line against cost-of-living increases, the overpayment and refund process is a poor substitute. Indeed, in this very case, after Tennessee had been directed to provide a refund for the period April 5—October 31, 1960 (and had been denied a stay, 283 F. 2d 729), Pittsburgh complained, without avail, in a motion filed with the Commission January 17, 1961, that much of the refund was not flowing through to consumers because of Tennessee's methods in disbursing the refund to the distributor companies.

Mr. Justice Douglas has pointed out (*United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division*, 358 U.S. 103, 119, dissenting opinion) and the Commission has recognized (*FPC Annual Report 1953*, p. 101) that the protection to consumers given by the refund provision of the Natural Gas Act is far from complete. Consumers are ambulatory, and in the years between the excess collection and the usual refund the consumer population for given areas invariably shifts. The administering of a refund at the consumer level is therefore not only something in the nature of an approximation, but also involves administrative detail and expense which comes out of and reduces the refund.

In the case of industrial consumers, as distinct from other consumers, since the Commission has no authority to suspend rates for resale for industrial use only, many of the industrial consumers do not have the benefit of a bond or obligation to refund for excessive rates collected, *Pacific Natural Gas Company v. Federal Power Commission*, 276 F. 2d 350 (9 Cir.); *Gas Service Company v. Federal Power Commission*, 282 F. 2d 496 (DC Cir.); *Mississippi Valley Gas Com-*

pany v. Federal Power Commission, — F. 2d — (5 Cir., No. 18501, Sept. 12, 1961). For these consumers, there is not even the imperfect protection of the refund obligation.⁷

Hence every legitimate step which the Commission can devise to accelerate partially, as well as in toto, the reduction of overstated rates and collections, in place of the less satisfactory, and less adequate, refund method, is in keeping with the letter and spirit of the Natural Gas Act, and deserving of judicial support.

⁷ While all of respondent Tennessee's rate increase schedules in the litigated docket appear to have been suspended, so that any industrial users of the gas coming thereunder may not necessarily lack refund protection, in certain pending cases where the FPC staff is desirous of having the interim order procedure applied, the industrial consumers do not have any refund obligation protection. An example is the pending *Cities Service Gas Company* rate increase, FPC Docket No. RP 62-1. Unless the cloud on the interim order procedure cast by the decision of the Court below in the instant case is removed by this Court, it is doubtful that the interim order procedure would be applied in the *Cities Service* case or any other case.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

DAVID W. CRAIG,
City Solicitor,
City of Pittsburgh, Pennsylvania.

CHARLES S. RHYNE,
HERZEL H. E. PLAINE,
Rhyme & Rhyme,
400 Hill Building,
Washington 6, D.C.

Attorneys for Petitioner, City of
Pittsburgh, Pennsylvania.

DECEMBER, 1961.

(254-3)

Office-Supreme Court, U.S.

FILED

DEC 20 1961

JOHN F. DAVIS, CLERK

IN THE
Supreme Court of the United States

No. ~~48~~
October Term, 1961

FEDERAL POWER COMMISSION,

Petitioner

VERSUS

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT AND HEAT
COMPANY, THE OHIO FUEL GAS COMPANY,
and UNITED FUEL GAS COMPANY

**BRIEF AMICUS CURIAE OF THE COMMON
WEALTH OF PENNSYLVANIA AND THE
PENNSYLVANIA PUBLIC UTILITY COMMIS-
SION, IN SUPPORT OF PETITION FOR A WRIT
OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE FIFTH
CIRCUIT**

HERBERT E. SQUIRES

Assistant Counsel

ALAN R. SQUIRES

Assistant Counsel

JOSEPH I. LEWIS

Counsel

For the Pennsylvania Public Utility
Commission

DAVID STAHL

Attorney General

Commonwealth of Pennsylvania

North Office Building
Harrisburg, Pennsylvania

INDEX

	Page
Interest of Amicus Curiae	1
Statement of the Case	3
Reasons for Granting the Writ:	
The Opinion of the Lower Court Raises the Question in What Circumstances the Commission Would Be Justified in Issuing its Interim Rate Order	4
A. The Commission Has Full Authority To Issue an Interim Rate Order Upon Compliance With the Mandates of the Act Which Have Been Judicially Established	4
B. The Commission Has Fully Complied With the Mandates of the Natural Gas Act	7
The Commission's Interim Reduction Order Was a Reasonable and Appropriate Exercise of Its Statutory Authority	9
Necessity For Upholding the Commission's Authority To Issue Interim Rate Orders	15

TABLE OF CITATIONS

CASES:

Federal Power Commission v. Natural Gas Pipeline Co., 315 U. S. 575	5, 12, 13
Los Angeles Gas Corp. v. Railroad Commission, 289 U. S. 287	12

Natural Gas Pipeline Co. v. Federal Power Commission, 120 F. 2d 625 (C. A. 7)	5, 14
Northern Natural Gas Co., 25 FPC Opinion No. 342, Nos. G-19040, et al, March 7, 1961	10
Panhandle Eastern Pipeline Co. v. Federal Power Commission, 236 F. 2d, 606 (C. A. 3)	5, 6
Panhandle Eastern Pipeline Co. v. Federal Power Commission, 143 F. 2d, 488 (C. A. 8)	12
State Corporation Commission of Kansas v. Federal Power Commission, 206 F. 2d, 690 (C. A. 8)	5

STATUTES:

Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821-833, as Amended, 15 U. S. C. 717-717W:	
Section 4, 15 U. S. C. 717c	4
Section 4(e) 15 U.S.C. 717c(e)	4, 5, 7, 8, 9, 10, 15
Section 5(a) 15 U.S.C. 717d(a)	11
Public Utility Law, Act of May 28, 1937, P. L. 1053, 66 Purdon's Penna. Statutes Annotated 1101	2

IN THE
SUPREME COURT OF THE UNITED STATES

No. 701
October Term, 1961

FEDERAL POWER COMMISSION,

Petitioner

vs.

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT AND HEAT
COMPANY, THE OHIO FUEL GAS COMPANY,
and UNITED FUEL GAS COMPANY

**BRIEF AMICUS CURIAE OF THE COMMON-
WEALTH OF PENNSYLVANIA AND THE PENN-
SYLVANIA PUBLIC UTILITY COMMISSION, IN
SUPPORT OF PETITIONS FOR A WRIT OF
CERTIORARI TO THE UNITED STATES COURT
OF APPEALS FOR THE FIFTH CIRCUIT.**

INTEREST OF AMICUS CURIAE

The Commonwealth of Pennsylvania and the Penn-
sylvania Public Utility Commission, an agency of the

Commonwealth, file this Brief pursuant to Rule 42(4) of the rules of this Court.

The Pennsylvania Public Utility Commission respectfully represents that it is a regulatory body of the Commonwealth of Pennsylvania, having jurisdiction to regulate rates and charges for the sale and distribution of gas pursuant to the Pennsylvania Public Utility Law, Act of May 28, 1927, P.L. 1053, 66 Purdon's Pennsylvania Statutes Annotated, 1101. This statute reposes in the Commission responsibility for the regulation of public utilities and for the preservation and protection of the public interest. The Pennsylvania Commission has an interest in any proceeding which affects the supply of natural gas and the rates charged to public utilities distributing gas within the Commonwealth of Pennsylvania.

Tennessee Gas Transmission Company is a major supplier of a number of such distributing companies and of their wholesale suppliers. The issues presented by the instant case, may have a substantial impact on the cost of gas to distributing companies and on the rates charged to ultimate consumers in Pennsylvania. Moreover, the outcome of such issues may affect action by the Federal Power Commission with respect to both pending and future proceedings involving rates of other natural gas companies supplying gas to distributing companies in Pennsylvania and their wholesale suppliers.

Because of the broad impact of any decision rendered in this case on the rates to be charged to ultimate consumers in Pennsylvania, we urge the Court to review the decision below. (Reported at 293 F. 2d 761).

STATEMENT OF THE CASE

The Petitions for Writ of Certiorari request that this Court review a decision of the Fifth Circuit Court of Appeals which sets aside an order of the Federal Power Commission requiring an immediate reduction in rates and the refunding of that part of the increased rates collected subject to refund and found by the Commission's order to be excessive.

The history of the proceedings commencing with the order of the Federal Power Commission and the subsequent review by the Circuit Court are set forth in the Petition for Writ of Certiorari submitted by the Federal Power Commission.

REASONS FOR GRANTING THE WRIT

THE OPINION OF THE LOWER COURT RAISES THE QUESTION IN WHAT CIRCUMSTANCES THE COMMISSION WOULD BE JUSTIFIED IN ISSUING ITS INTERIM RATE ORDER

A. The Commission has full Authority to issue an interim rate order upon compliance with the mandates of the Act which have been judicially established.

The opinion of the lower court casts doubt upon both the authority of the Commission to issue an interim rate order and the legality of such an order where issues of cost allocation are unresolved. It is our contention that the Court's opinion rests on faulty reasoning and is contrary to established principles of law.

The Commission's authority generally to issue interim rate orders is derived from Sections 4 and 5 of the Natural Gas Act, June 21, 1938, 52 Stat. 822; Title 15 U.S.C. 717(e).

Section 4 (e) states in part:

"After a full hearing . . . the Commission may make such orders with reference thereto (i.e., change in rate, charge, classification or service) as would be proper in a proceeding initiated after it had become effective. . . .¹ Where increased

¹ This section incorporates all the powers conferred upon the Commission by Section 5(a) of the Natural Gas Act.

rates or charges are thus made effective (i.e., at the expiration of the suspension period on motion of the natural gas company making filing of a change in rate), the Commission may . . . upon completion of the hearing and decision [to] order such natural gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified."

The mandates contained in Section 4(e) require a full hearing and decision. These mandates have been judicially defined in *Pankandle Eastern Pipeline Co. v. Federal Power Commission*, 236 F. 2d 606 (C.A. 3); *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F. 2d 690 (C.A. 8), cert. den. 346 U.S. 922; and *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U.S. 575, 585.

In *Natural Gas Pipeline Company v. Federal Power Commission*, 420 F. 2d 625, the Circuit Court discussed the right of the Commission to issue an interim order and in so doing indicated the timeliness of such action: •

"We must, and do, hold that upon a proper showing, and when the hearing has reached a stage where the Commission may determine that a reduction (or an increase) of rates should be made, it may (and should) make such order, even though the hearing be not completed."

The Supreme Court, on review, *Federal Power Commission v. Natural Gas Pipeline Company*, supra, affirming the right of the Commission to issue an interim rate order also set forth what constituted a full hearing. There the Court held (315 U.S. 583-584):

"... while the proceedings were not ended by the interim order, the companies had full opportunity to offer all their evidence both direct and in rebuttal, and full opportunity to cross-examine every witness offered by both the Federal Power Commission and the Illinois Commerce Commission. All the evidence tendered was received and considered by the Commission, and before the interim order was entered counsel for the companies stated to the Commission that they had concluded the direct testimony in support of their case. So far as the order is supported by the evidence the companies cannot complain that they were denied a full hearing because they had not been able to examine or redirect their own witnesses who had not been cross-examined, or because they had no opportunity to cross-examine or rebut witnesses who were not offered by the Commission. The right to a full hearing before any tribunal does not include the right to challenge or rely on evidence not offered or considered."

In *Panhandle Eastern Pipeline Co. v. Federal Power Commission*, supra, the utility objected to the Commission's order on the ground that a full hearing was not granted. The Third Circuit held (236 F. 2d at 608):

"Here the record shows that Panhandle was given full opportunity to offer all of its evidence in support of the items which the commission disallowed in the order now on appeal. Thereafter, the commission was under no obligation to postpone its ruling on those matters. Indeed, to have

done so would have permitted Panhandle to put into effect . . . increased rates, parts of which it had attempted and, in the commission's view, failed to justify."

It is apparent from the above authorities that the mandate requiring a "full hearing" is satisfied when the proponent of an increased rate has been permitted to introduce all of its evidence in chief on the issue or issues disposed of by the Commission's interim order.

B. The Commission has fully complied with the mandates of the Natural Gas Act.

The lower Court questions whether a "full hearing" had been afforded to Tennessee in accordance with the mandate of Section 4(e) of the Act. Tennessee was permitted to present its entire case. Its witnesses were cross-examined on the rate of return issue. Thereafter, other parties to the proceeding presented evidence on rate of return with subsequent cross-examination. Tennessee then presented rebuttal testimony on rate of return, on which there was cross-examination.

The Commission, accepting the determination by the examiner that there was no further evidence to be presented on rate of return, heard oral argument on this issue, as well as on whether interim rate reductions and refunds should be ordered.

The Commission considered Tennessee's entire presentation including its cost allocation methods, and issued its interim order thereon. All of the evidence having been introduced, the Commission was certain-

ly under no obligation to reserve its decision on rate of return until all other issues in the proceeding had been resolved. Tennessee cannot complain of injury as a result of the interim order if it has failed to justify the increased rates on the basis of its own theory and evidentiary presentation.

We submit that the Commission, having allowed Tennessee a full hearing with opportunity to present its case in chief, and having issued an interim order on the completed record, has fully complied with the mandates of Section 4(e) of the Act.

THE COMMISSION'S INTERIM REDUCTION ORDER WAS A REASONABLE AND APPROPRIATE EXERCISE OF ITS STATUTORY AUTHORITY

Section 4(c) of the Natural Gas Act provides, *inter alia*:

"At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable, shall be upon the natural gas company . . ."

The plain meaning of this language is that the natural gas company must sustain the burden of proof and justify the entire amount of any rate increase. This burden cannot under any circumstances be shifted to the Commission. Should the natural gas company, after full hearing, not sustain this burden for the requested rate increase, the Commission is then empowered to order a refund by the natural gas company of that portion of the requested increase not justified:

In the instant case, Tennessee's evidence supported a rate of return of 6½% as compared to the requested rate of 7%. Therefore, the Commission was fully authorized to disallow the amounts claimed, but not justified by Tennessee. Moreover, the Commission was under no duty to show that any portion of the disallowed rates would be justified by further evidence on other issues in the proceeding.

The majority of the Circuit Court was of the opinion that the Commission's failure to resolve all issues

affecting the determination of just and reasonable rates would deprive Tennessee of the process of law and threaten them with irreparable harm should the ultimate rates established be in excess of the rates set by the interim order.

Our answer to this assertion is twofold. First, as has been previously noted, Tennessee had the burden of proof to justify the requested increase. The full hearing, as above defined, on this issue and the subsequent decision by the Commission based thereon, satisfied the requirements of procedural due process in accordance with Section 4(c) of the Act.

Second, the Court's apparent alarm with regard to the threat of irreparable injury to Tennessee is conjectural and does not support the conclusion that the Commission abused its discretion. The fears expressed reach out to cast the Commission's action in a light having the worst possible effect on Tennessee's revenues.

The Court has failed to give any consideration to the protections afforded Tennessee by the cost of service issues yet to be decided in this proceeding and other proceedings affecting Tennessee's suppliers. Thus, the speculative consequences predicted, ignore the fact that Tennessee pays large amounts for its gas supply subject to possible refund, and they likewise ignore the fact that the allowance of 6½% to Tennessee does not reflect the Commission's present policy of allowing a return of only 1½% on the company's reserve for accumulated deferred taxes.²

² See: *Northern Natural Gas Company et al.*, Docket G.19940 et al., Opinion No. 342, March 7, 1961, wherein the

Furthermore, the Court overlooked the fact that in practically every rate case the Commission makes substantial reductions in the claimed cost of service for items other than the rate of return.

In view of the foregoing, we submit that Tennessee's revenues already contain substantial amounts which will be available to meet any revenue requirement adjustments found necessary as a result of possible changes in the cost allocation method.

Notwithstanding the possibility that the Commission's final order on cost allocation may indicate that Tennessee is entitled to receive greater revenues than those collected under the interim order rates, we submit that Tennessee does not have a vested right to a 7% return which would be produced by their filed rates nor does Tennessee have a vested right to the overall revenues which would produce a 6½% return. Although the Commission's order found a 6½% return to be a just and reasonable return for Tennessee, which finding was affirmed by the lower Court, it is within the Commission's discretion to order rate decreases to the lowest reasonable rates.

Section 5(a) of the Act states:

"... the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates."

Commission included in the cost of capital determination the reserve for accumulated deferred taxes at a return of 1½%. The Commission was of the opinion that a return of 1½% of moneys in the deferred tax account was a sufficient incentive to a regulated company to induce it to take advantage of the provisions of Section 167 of the Internal Revenue Code.

By long standing usage in the field of rate regulation the "lowest reasonable rate" is one which is not confiscatory in the constitutional sense.³

In this connection, the Court of Appeals for the Eighth Circuit stated in *Panhandle Eastern Pipeline Co. v. Federal Power Commission*, 143 F. 2d 488, 496:

"The last question for consideration is whether the return allowed by the Commission has been shown to be unjust, unreasonable or confiscatory.

"The opinion of the Supreme Court in the *Hope Natural Gas Company* cases indicates to us that, aside from questions relating to procedural due process and to jurisdiction, a reviewing court may interest itself only in the effect of the Commission's order. The court cannot concern itself with the Commission's choice of formulae or the propriety of the methods employed by it in reaching its conclusion, but only with the consequences of the order made. If the effect of the order is to deny to the utility a return sufficient reasonably to meet its necessities and to enable it to continue to render adequate public service, the order is arbitrary and confiscatory and may be set aside. It seems apparent that the Supreme Court is presently of the opinion that, within broad limits, the Federal Power Commission should be freed from judicial interference in regulating rates of natural-gas companies. It is evidently no longer necessary for a reviewing court to consider many

³ See: *F.P.C. v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585; *Los Angeles Gas Corp. v. Railroad Commission*, 289 U.S. 287, 305.

of the doubtful and debatable questions which ordinarily arise in every rate case.

"The order of the Commission must be affirmed unless the petitioners have made a convincing showing that it is unreasonable in its consequences because the return allowed is insufficient to enable them to meet their expenses of operation, to pay interest on their bonds and dividends on their stock, to maintain their credit and to attract capital or is clearly out of line with the returns on investments in enterprises involving comparable risks."

If we assume, arguendo, that Tennessee fails to earn a 6½% return under the rates established by the interim order, no injury may be claimed unless the overall return is reduced to the level of confiscation.

On this point, the Supreme Court in *F. P. C. vs. Natural Gas Pipeline Co.*, supra, stated:

"Assuming that there is a zone of reasonableness within which the Commission is free to fix a rate varying in amount and higher than a confiscatory rate, the Commission is also free under Sec. 5(a) to decrease any rate which is not the 'lowest reasonable rate'. It follows that the congressional standard prescribed by this statute coincides with that of the constitution, and that the courts are without authority under the statute to set aside as too low any 'reasonable rate' adopted by the Commission which is consistent with constitutional requirements."

The lower Court, in the present case, invalidates the Commission's interim order on the assumption that

the retroactive effect of the final determination of the cost allocation issue will make it "highly unlikely, if not impossible, for a utility to earn a 'just and reasonable return'."

The Court not only fails to lay any foundation for this assumption, but has acted without the legal criteria declared necessary by this Court in the *Natural Gas Pipeline* case, *supra*.

We submit that the various means of protection available to Tennessee, coupled with the legal principles that rates not shown to be confiscatory cannot be set aside, clearly indicate that the reasoning of the Court below on the interim order issue is contrary to both fact and legal precedent and can not be sustained.

NECESSITY FOR UPHOLDING THE COMMISSION'S AUTHORITY TO ISSUE INTERIM RATE ORDERS

The Commission's interim rate order procedure is of great significance and import in effectuating the purposes which the legislature sought to accomplish with the passage of the Natural Gas Act. The primary purpose of the Act is to protect the consumer interests against exploitation at the hands of private natural gas companies.

The decision of the Court below would deny to the Commission a procedure (interim rate orders) to decide increased rate questions "as speedily as possible" in accordance with the mandate of Section 4(e) of the Natural Gas Act. Thus, the natural gas companies would be enabled to continue to collect excessive rates. Under the circumstances, consumer interests would not be fully protected as was intended by the Act.

Moreover, while the consumers are entitled to refunds of excess rates charged, together with seven percent (7%) interest, such a protection is not effective unless the Commission is permitted to dispose of its rate cases with rapidity. Unless reduced rates and refunds are ordered as soon as it is feasible, inequities will result in that those who benefit by the final determination will not necessarily be those rate payers who contributed the excessive amounts.

Public utility rate cases are invariably intricate and protracted and often involve various difficult issues.

Although some issues require extensive study and investigation, others can be determined fairly promptly. The Commission, in recent months, has been grasping for methods and means of alleviating the regulatory lag and the resultant large sums of money which the natural gas companies have been collecting from their customers subject to refund. The interim order procedure is one of the Commission's methods of providing this prompt relief to the consumers of natural gas.

The effect of this decision upon the regulation of an industry which is growing by leaps and bounds, and the efforts of the Commission to afford expeditious relief to consumers of natural gas, is of such extreme importance that to abandon the interim order procedure would be a step in the wrong direction.

RESPONDENT'S BRIEF IN OPPO- SITION

Office Supreme Court, U.S.
FILED

JAN 8 1962

AVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

~~Nos. 434 and 605~~

FEDERAL POWER COMMISSION,

Petitioner.

TENNESSEE GAS TRANSMISSION COMPANY, THE
MANUFACTURERS LIGHT AND HEAT COMPANY,
THE OHIO FUEL GAS COMPANY AND UNITED FUEL
GAS COMPANY,

Respondents.

CITY OF PITTSBURGH,

Petitioner.

TENNESSEE GAS TRANSMISSION COMPANY, THE
MANUFACTURERS LIGHT AND HEAT COMPANY,
THE OHIO FUEL GAS COMPANY AND UNITED FUEL
GAS COMPANY,

Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF
APPEALS FOR THE FIFTH CIRCUIT

**BRIEF FOR RESPONDENTS, THE MANUFACTURERS
LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS
COMPANY AND UNITED FUEL GAS COMPANY
IN OPPOSITION TO PETITIONS FOR
WRITS OF CERTIORARI**

BROOKS E. SMITH
FREDERICK H. CLARK
GILES D. H. SNYDER
120 East 41st Street
New York 17, New York

Counsel for

*The Manufacturers Light and
Heat Company, The Ohio
Fuel Gas Company and
United Fuel Gas Company*

WILLIAM ANDERSON
EDWARD B. CALLAND
800 Union Trust Building
Pittsburgh 19, Pennsylvania

Counsel for

*The Manufacturers Light and
Heat Company*

R. K. TALBOTT
HERBERT W. BRYAN
1700 MacCorkle Avenue, S.E.
Charleston 25, West Virginia.

Counsel for

United Fuel Gas Company

W. F. LAIRD
RALPH N. MAHAFFEY
99 North Front Street
Columbus 15, Ohio

Counsel for

The Ohio Fuel Gas Company

INDEX

	PAGE
OPINIONS BELOW	2
QUESTION PRESENTED	2
STATUTES INVOLVED	3
STATEMENT	3
A. The Controversy of Undue Rate Discrimination Was Raised Several Years Before Tennessee Filed for a 7 per cent Rate Of Return	4
B. The G-19083 Hearing Before the Commission	6
ARGUMENT AGAINST GRANTING WRITS	6
I. The Decision of the Court of Appeals Is Cor- rect	6
II. There Is No Conflict Of Decision	9
III. It is Important That The Decision Below Stand	12
IV. The Petitions Raise Matters Extraneous to the Record	13
CONCLUSION	15
APPENDIX A	16

TABLE OF CITATIONS

CASES:

<i>Cobbledick, et al. v. U. S.</i> , 309 U. S. 323, 325 (1940)	15
<i>F. P. C. v. Natural Gas Pipeline Co. of America</i> , 315 U. S. 575 (1942)	9, 10, 11
<i>Panhandle Eastern Pipe Line Co. v. Federal Power Commission</i> , 236 F2d 606 (1956, CA3)	9, 11
<i>State Corporation Commission of Kansas v. Federal Power Commission</i> , 206 F2d 690 (1953, CA8), cert. den. 346 U. S. 922	10, 11, 12

STATUTES AND REGULATIONS

	PAGE
<i>Administrative Procedure Act</i> —(5 USC §§ 1001-1011)	
Section 5(b)—(5 USC § 1004(b))	7
Section 7(c)—(5 USC § 1006(c))	7
Section 7(d)—(5 USC § 1006(d))	7
Section 8(b)—(5 USC § 1007(b))	7
Section 12—(5 USC § 1011)	7
<i>Natural Gas Act</i> —(15 USC §§ 717a-717w)	
Section 4—(15 USC § 717c)	7
Section 4(b)—(15 USC § 717c(b))	4
Section 4(c)—(15 USC § 717c(e))	11
Section 5—(15 USC § 717d)	7
Section 5(a)—(15 USC § 717d(a))	4, 9, 10

IN THE
Supreme Court of the United States

OCTOBER TERM, 1961

FEDERAL POWER COMMISSION,

Petitioner,

v.

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT AND HEAT
COMPANY, THE OHIO FUEL GAS COM-
PANY AND UNITED FUEL GAS COMPANY;

Respondents.

Nos. 591
and 605

CITY OF PITTSBURGH,

Petitioner,

v.

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT AND HEAT
COMPANY, THE OHIO FUEL GAS COM-
PANY AND UNITED FUEL GAS COMPANY;

Respondents.

**BRIEF FOR RESPONDENTS, THE MANUFACTURERS
LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS
COMPANY AND UNITED FUEL GAS COMPANY
IN OPPOSITION TO PETITIONS FOR
WRITS OF CERTIORARI**

Respondents, The Manufacturers Light and Heat Com-
pany, The Ohio Fuel Gas Company, and United Fuel Gas
Company (Columbia Companies) oppose the grant of writs
of certiorari to review the judgment of the United States

Court of Appeals for the Fifth Circuit sought by petitions filed on December 8 and 11, 1961, by the Federal Power Commission and the City of Pittsburgh, respectively, and the brief *amicus curiae* of the Commonwealth of Pennsylvania and the Pennsylvania Public Utility Commission.

OPINIONS BELOW

The Opinions of the Court of Appeals for the Fifth Circuit are reported at 283 F2d 729 and 293 F2d 761. The opinion at 283 F2d 729 is the Court's denial of Respondents' motions for a judicial stay of the underlying administrative order. This opinion is pertinent to a full understanding of the effect of the Court's opinion on the merits at 293 F2d 761 of Respondents' petitions for review of the underlying administrative order. The Orders of the Federal Power Commission (Commission) are reported at 24 FPC 204 and 525.

QUESTION PRESENTED

Columbia Companies cannot agree with the scope or content of Petitioners' "Question Presented" sections. A more accurate statement follows.

Respondent natural gas company and its customers, including respondents Columbia Companies, have an unresolved controversy of long standing pending before the petitioner Commission in a prior collateral proceeding involving (a) the propriety of the natural gas company's method of allocating its cost of service among zones and classes of service within each zone and (b) the related issue of undue rate discrimination whereby certain customers are overcharged and other customers are undercharged. The determination of this controversy will substantially affect pending rate filings by the natural gas company and the proportions of its costs which will be borne by various

customers purchasing gas under a variety of classes of service in six rate zones.

The question which arises under this fact situation and Sections 4 and 5 of the Natural Gas Act and Sections 5, 7, 8 and 12 of the Administrative Procedure Act is whether it is an abuse of discretion for the Commission to order immediate rate reductions without a full hearing and decision upon a method of cost allocation being contested by customers of the natural gas company upon the finding that the rate of return cost them in a natural gas company's cost of service is excessive.

STATUTES INVOLVED

In addition to the pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U. S. C. 717-717w, set out in Appendix B to the Petition of the Federal Power Commission, the pertinent provisions of the Administrative Procedure Act, 60 Stat. 237, 5 U. S. C. 1001-1011, are set out in Appendix A *infra*, pages 16-18.

STATEMENT

For purposes of brevity, Columbia Companies at this stage of the proceeding adopt the statement set forth in the Petition of the Federal Power Commission, pages 3 to 8, with certain important exceptions and additions.

Tennessee Gas Transmission Company (Tennessee), the natural gas company whose rates are involved in the underlying administrative proceeding, transports and sells large amounts of gas to Columbia Companies in Tennessee's rate Zones 2 (Kentucky), 3 (West Virginia) and 4 (Ohio and Pennsylvania). Tennessee has three other rate Zones 1 (Texas), 5 (Kentucky), 6 (New York) and 7 (New England). Tennessee performs a variety of natural gas

services in these six rate zones to scores of wholesale customers who, in turn, sell gas to ultimate consumers and or to other companies for resale.

A. *The Controversy of Undue Rate Discrimination Was Raised Several Years Before Tennessee Filed for a 7 per cent Rate Of Return.* Tennessee expanded its service in its terminal Zones 1, 5 and 6 (including new markets in New York and New England) during the 1952-1958 period without substantial expansion of service to Columbia Companies. Contemporaneously, it filed successive rate increases which fell disproportionately upon Columbia Companies and other customers located in Zones 2, 3 and 4. Columbia Companies have steadfastly and strenuously complained to the Commission of undue rate discrimination in violation of Sections 4(b) and 5(a) of the Natural Gas Act.

Columbia Companies and others have complained that a basic cause of this discrimination is Tennessee's method of allocating its cost of service to zones and classes of service. This unresolved issue has been pending before the Commission in several administrative proceedings prior to the proceeding at Docket No. G-19983 which was reviewed by the Fifth Circuit. The issue has been handled by the Commission in the following manner:

1. *Docket No. G-5259.* Tennessee filed for rate increases in 1954. In an order issued October 6, 1955, the Commission recognized the controversy involving zone cost allocation and rate design. (R. 622) However, the cost allocation issue was not determined because that docket was settled. By order issued September 5, 1957, the Commission noted that the zoning issue was to be presented in the next succeeding rate case, Docket No. G-11980. (R. 622).

2. *Docket No. G-11980.* The rate increases in this proceeding became effective subject to refund on July 14,

1957. The Commission made it clear that its determination of principles and methods of cost allocation would extend to subsequent cases. (R. 609-610) The controversy in G-11980 is still pending before the Commission after oral argument on exceptions to the Examiner's decision. None of the cost of service issues in this prior case have been determined. All phases of this proceeding are awaiting final administrative action.

3. *Docket No. G-17166.* Tennessee filed a "second layer" of rate increases (in addition to the G-11980 increments) effective May 15, 1959, subject to refund. No action has been taken by the Commission in this case, since the Commission, in effect, by passed it to hold hearings on the "third layer" rate case, Docket No. G-19983.

4. *Docket Nos. G-11107 and G-15826.* These were certificate cases in which, among other things, Tennessee sought Commission approval for peaking service rates which Columbia Companies contend aggravated an already existing rate preference in favor of Tennessee's customers in its Zones 5 and 6 in New York and New England. These cases are still pending before the United States Court of Appeals for the District of Columbia Circuit, Case Nos. 14897 and 15160. On September 21, 1959, that Court ordered these cases to be held in abeyance until further order of the Court. Obviously, that Court is awaiting the outcome of the controversy in Docket Nos. G-11980, et al.

5. *Docket No. G-19983.* Tennessee filed increased rates which became effective subject to refund on April 5, 1960. These rates remained in effect until November 1, 1960, and have since been superseded by lower rates pursuant to the Commission's order of August 9, 1960. The Fifth Circuit reviewed this order and ruled that "regardless of the Commission's authority to issue the order, we hold that cost allocation among zones is such an essential element in deter-

6
mining whether the filed rates are excessive that it is an abuse of discretion to issue an interim rate order before deciding a pending allocation issue ripe for decision." (R. 683-684)

B. *The G-19983 Hearing Before the Commission.* In the hearing below in Docket No. G-19983, none of the intervenors, including Columbia Companies, were permitted to introduce evidence on cost allocation. (R. 50-54, 291-295, 378-379)

The Commission was fully informed of the Examiner's refusal to permit such evidence. (R. 577-583, 607-625)

Although Commission Staff counsel "contemplated acceptance" by the parties to Tennessee's methods "for purposes of an interim order" in Docket No. G-19983, certain intervenors, including Columbia Companies, were *not* willing to accept Tennessee's methods for such purposes. Such methods had been and are being vigorously contested before the Commission in a prior proceeding, Docket No. G-11980, as well as being opposed in the underlying proceeding, Docket No. G-19983, for use by the Commission to lower rates which may already have been too low for certain localities and classes of service.

ARGUMENT AGAINST GRANTING WRITS

I. The Decision of the Court of Appeals Is Correct.

The Court of Appeals did not deny the authority of the Commission to issue interim rate orders in the proper case. It merely held that in this case it was "unreasonable and an abuse of discretion to issue an interim rate order before deciding a pending allocation issue ripe for decision." (R. 683-684)

The Court of Appeals recognized that both the filing company, Tennessee, and the intervening customer

Commission can eliminate what it finds to be an unlawful increment in the price structure. See *State Corporation Com. of Kansas v. F. P. C.*, 8 Cir., 206 F.2d 690, cert. den. 346 U. S. 922."

By necessary implication, the majority of the Court believed that Columbia Companies were not to be relegated to a position of secondary priority in getting *their* "day in court" before the administrative tribunal. In contrast to the Fifth Circuit, Petitioners imply that only Tennessee, and not Columbia Companies, have procedural rights under the statutes. (See Commission Petition page 7; Pennsylvania brief page 9).

Columbia Companies submit that Petitioners' position is grounded in a fundamental misconception of the rate-making process for a natural gas company having a complicated zonal rate structure. Petitioners would take the determination of a lower "rate of return" (which fixes only one *cost* item in an over-all cost of service made up of many items) and translate aggregate lower *costs* directly into *rates*.* There are other steps in the rate-making process which come after the items of a cost of service are determined. These subsequent steps include cost allocation and rate design which are equally important and include a determination of the various portions of the total cost of service which each customer should share. This Court has recognized that there are steps of different character which are taken to establish rates for a regulated industry. The first step is to ascertain costs. A separate and distinct step

*Tennessee's claimed jurisdictional cost of service with a 7 per cent rate of return cost item is \$24,537,001. With a 6 1/2 per cent rate of return the Commission asserts that these annual costs are reduced by over \$11,000,000. (R. 590.) Obviously then, this cost item is significant because on the final determination of Tennessee's rates, as applied to zones it can be used to remove the inequities that exist because of undue rate discrimination.

is to make adjustments "so as to eliminate discriminations and unfairness. . . ." *F. P. C. v. Natural Gas Pipeline Co. of America*, 315 U. S. 575, 584, 62 S. Ct. 736, 742 (1942).

Petitioners apparently believe that for an interim period the Commission could by-pass an essential step by using a contested method of cost allocation. The Court of Appeals believed otherwise. The Court held that cost allocation among zones was an essential element in determining whether or not Tennessee's rates are too low or too high as to each customer.

Moreover, Petitioners state that the effect of the Commission's order requiring interim rates on the basis of a cost of 6.8% per cent rate of return and Tennessee's allocation methods would put Tennessee's customers in the same position as if Tennessee had originally filed rates on the basis of a 6.8 per cent rather than a 7 per cent rate of return. This is an erroneous concept. Columbia Companies submit that when Tennessee voluntarily filed higher rates in Zones 1, 5 and 6 for whatever combination of reasons, the customers in Zones 2, 3 and 4 were benefited substantially. This is so because the Commission lacks the authority under Section 5(a) of the Natural Gas Act to *compel* a natural gas company to *increase* its effective rates. Thus, when Tennessee voluntarily filed higher rates, it was a step which would tend to help correct the undue rate preference which Columbia Companies contend Tennessee has been giving its customers in Zones 1, 5 and 6.

II. There Is No Conflict Of Decision.

Petitioners assert that the decision in the instant case somehow conflicts with the ruling of this Court in *F. P. C. v. Natural Gas Pipeline Co. of America*; *supra*, and with the decision by other courts of appeal in *Vanhondt Eastern Pipe Line Co. v. Federal Power Commission*, 236 F.2d 606

(1956, CA 3), and *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F.2d 690 (1953, CA 8), certiorari denied 346 U. S. 922.

While the cited cases involved interim rate orders, it is clear that the decision of the Fifth Circuit is consistent and does not conflict therewith. The Fifth Circuit held that the interim order procedure is improper under the circumstances existing in this case. Contrary to Petitioners' allegations, such procedure remains a tool available to the Commission if properly used.

No case cited by Petitioners involved a deferred cost allocation issue which could be applied retroactively to alter the results of the Commission's interim rate order. For example, the *Natural Gas Pipeline Co.* case, *supra*, related to a rate investigation by the Commission under Section 5(a) of the Natural Gas Act. The reduction of the company's rates to reflect the Commission's finding of a lower rate of return was final and could not be altered on a retroactive basis, since the Commission's power under Section 5 of the Act is restricted to orders having prospective effect only. Thus, a subsequent determination by the Commission of another issue could not operate to vary the result of the interim order.

In that case this Court was not asked to pass upon the propriety of the interim order procedure; rather, certain parties merely contended that "the order is invalid because the Commission did not itself fix reasonable rates as required by the Act but instead merely directed the companies to file a new rate schedule which would result in the prescribed reduction in operating revenues." (315 U. S. at 583) Since the appropriateness of the interim order procedure was not questioned under the factual circumstances of that case, as was done in the instant proceeding, there clearly can be no conflict of decision.

Also of importance is the fact that the *Natural Gas Pipeline Co.* case did not even touch upon the problems of cost allocation among rate zones and rate design. Thus, that case did not involve the important issues that were before the Commission below and reviewed by the Fifth Circuit. Moreover, not only is the *Natural Gas Pipeline Co.* case clearly distinguishable on this ground, but also it is authority for the proposition that parties must have "full opportunity to offer all their evidence both direct and in rebuttal, and full opportunity to cross-examine every witness. . . ." (315 U. S. 583-584) Columbia Companies did not have this opportunity in Docket No. G-10983, and the controlling collateral case, Docket No. G-11980 is still pending before the Commission.

The *Panhandle* case, *supra*, likewise did not involve a deferred cost allocation issue which could be applied retroactively to disturb the Commission's interim order. To the contrary, it appears from the Court's decision that the problem of zone allocation had already been decided prior to the issuance of the interim order. (236 F2d at 611)

The issue in the *Panhandle* case was completely unrelated to the problem involved in the instant proceeding. Panhandle's objection before the Third Circuit did not relate to the effect of some deferred issue upon the interim order. The company merely asserted that the order was invalid since it prevented the parties from making a supplementary showing as to recent developments and changes in circumstances occurring during the pendency of the total rate proceeding. (236 F2d at 608).

State Corporation Commission of Kansas v. Federal Power Commission, supra, involved a natural gas system which was not even zoned at the time the Commission issued the interim order under review. Certain parties to the proceedings had presented evidence proposing zone rates.

The Commission declined to decide the question due to the inadequacy of the evidence and designated a subsequent case, Docket No. G-1881, as being appropriate for the exploration of the problem of zone rates. (206 F2d at 712)

Since the Commission determined that the problem of zone rates should be decided in a separate future proceeding, it is clear that its interim order could not be affected thereby and could be considered final as to the issues decided.

Moreover, an examination of the opinion by the Eighth Circuit indicates that no objection was raised as to the propriety of the interim order procedure as such under the facts of that case. The company involved, Northern Natural Gas Company, apparently made no showing as to any possible harm that could flow to it, retroactively or otherwise, as a result of the interim order, judging from the Court's statement that "We are not shown any particular in which Northern was prejudiced by the Commission's action. . . ." (206 F2d at 716)

Clearly, the facts and issues in the present case are quite different from those which existed in the decisions relied upon by Petitioners. It cannot be validly asserted, therefore, that the decisions are at variance.

Columbia Companies submit that there is no conflict in decision or principle—either direct or indirect—upon which this Court could issue the writs sought. The cases cited by Petitioners are fully and substantially distinguishable from this case.

III. It is Important That The Decision Below Stand.

Columbia Companies (and Tennessee) unsuccessfully sought a judicial stay of the interim rate reduction and refund order of the Commission. The Fifth Circuit's order denying stay was issued October 28, 1960. (R. 630-632)

As a result of this denial Tennessee has reduced its rates as of April 5, 1960, which lower rates are still in effect as of the present time.* In addition Tennessee made refunds for the period from April 5, 1960 through October 31, 1960. Thus, there has been no correction of the undue rate preference granted Zones 1, 5 and 6 by Tennessee and aggravated by the interim reductions in those zones. In this situation prevails and cannot be corrected except for the future. It is important, therefore, that the decision by the Fifth Circuit take effect as soon as possible so that the Commission will permit Tennessee to raise higher rates for those zones to be effective prospectively.

IV. The Petitions Raise Matters Extraneous to the Record.

Columbia Companies submit that the proponents of the Petitions reveal the weakness in their position by the very fact of the extreme charges they make against the natural gas industry as a whole and their excursion into matters entirely extraneous to the record and irrelevant to the problem which the Court of Appeals decided.

For example, after prejudging rate increases filed by natural gas companies as "excessive," the contention is made that revenues from excessive rate increases are used as a "relatively cheap source of expansion capital." (Commission Petition, page 11) This generality is false. Natural gas companies do not deliberately overfile as the Commission implies. It would be most unwise for a natural gas company to do so. If it did, charges which would be ordered to be refunded after Commission consideration would not be available for investment in full, since about *half* of such overcol-

*Respondent, The Manufacturers Light and Heat Company, Inc., passed through refunds to Pennsylvania customers and has adjusted its rates accordingly to reflect the lower interim rates of Tennessee. The implications to the contrary on pages 4 and 16 of the Petition of City of Pittsburgh are in error.

lections would be paid out as income taxes. However, 7 per cent interest must be paid on the *total* amount of refund whether money refunded had been available for investment or not. This is a significantly higher capital cost than that applicable to debt capital of almost all pipelines, even after taxes.*

Thus, for example, if there was an overcharge of \$1,000,000, only \$500,000 would be available for investment for expansion. This \$500,000 "investment" would require interest at 14 per cent to cover the 7 per cent interest on a \$1,000,000 refund. This is a high cost of money in view of the Commission's determination that Tennessee is entitled to only $6\frac{1}{8}$ per cent rate of return over-all and slightly over 10 per cent on equity.

As an additional example of the extremes to which Petitioners go, the City of Pittsburgh raises the admittedly irrelevant fact that under Section 4(e) of the Natural Gas Act the Commission has no authority to suspend the rates for sale of gas for resale for industrial use only. (Pittsburgh Petition, pages 16-17, fn. 7).

Likewise, the rate case statistics cited by Petitioners in attempting to fabricate a reason that would persuade this Court to take jurisdiction are irrelevant to *this* case.

Columbia Companies appear before the Commission continuously in certificate and rate proceedings of their own and are most interested in administrative speed. However, the statutes under which the Commission and administrative litigants operate require that administrative action be *deliberate* on evidence presented as well as quick. Otherwise, there is no reason for the decisional process on a full evidentiary hearing granted to all interested parties.

Columbia Companies submit that the effect of the Petitions is an attempt to get this Court to rewrite the

*The interest rates on pipeline bonds and debentures rarely exceed 534 per cent (an effective rate of about 2875 per cent for corporations in the 52 per cent tax bracket).

controlling statutes by creating a judicial precedent which would nullify the clear provisions of the Natural Gas Act and Administrative Procedure Act. Congress has the law-making function and it has not seen fit to change the statutes so as to radically change the administrative process by approving administrative fiat and inequality of treatment of litigants. Columbia Companies support speed in the administrative process but only on condition that due process of law is not destroyed thereby. The interim order procedure is a valuable tool in some proceedings and circumstances but not in the case below.* An even better tool would be a quick determination of all issues in each rate case by such things as the use of conference and settlement techniques.

It is submitted that matters extraneous to *this* case and involving other companies and other rate cases are not a proper ground for the Court to grant writs of certiorari herein.

CONCLUSION

For the foregoing reasons it is respectfully submitted that the Petitions for the writs of certiorari should be denied.

Respectfully submitted,

BROOKS E. SMITH

January 8, 1962

*Even though interim rate orders are sometimes proper, there are numerous basic evils in piecemeal rate regulation occasioned by delays in final determinations before the administrative body and, if contested, delays due to a multiplicity of piecemeal judicial reviews. (Cf. *Cobbledick, et al. v. U. S.*, 300 U. S. 323, 325 (1940).)

APPENDIX A

The Administrative Procedure Act, 60 Stat. 237, 5 U. S. 1001 *et seq.*, provides, in pertinent part, as follows:

Section 5(b) "The agency shall afford all interested parties opportunity for (1) the submission and consideration of facts, arguments, offers of settlement, or proposals of adjustment where time, the nature of the proceeding, and the public interest permit, and (2) to the extent that the parties are unable so to determine any controversy by consent, hearing, and decision upon notice and in conformity with sections 1006 and 1007 of this title." (5 U. S. C. § 1004(b), June 11, 1946, c. 324, § 5, 60 Stat. 239)

Section 7(c) "Except as statutes otherwise provide, the proponent of a rule or order shall have the burden of proof. Any oral or documentary evidence may be received, but every agency shall as a matter of policy provide for the exclusion of irrelevant, immaterial, or unduly repetitious evidence and no sanction shall be imposed or rule or order be issued except upon consideration of the whole record or such portions thereof as may be cited by any party and as supported by and in accordance with the reliable, probative, and substantial evidence. Every party shall have the right to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts. In rule making or determining claims for money or benefits or applications for initial licenses any agency may, where the interest of any party will not be prejudiced thereby, adopt procedures for the submission of all or part of the evidence in written form." (5 U. S. C. § 1006(c), June 11, 1946, c. 324, § 7, 60 Stat. 241)

Section 7(d) "The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, shall constitute the exclusive record for

decision in accordance with section 1007 of this title and, upon payment of lawfully prescribed costs, shall be made available to the parties. Where any agency decision rests on official notice of a material fact not appearing in the evidence in the record, any party shall on timely request be afforded an opportunity to show the contrary." (5 U. S. C. § 1006(d), June 11, 1946, c. 324, § 7, 60 Stat. 241)

Section 8(b) "Prior to each recommended, initial, or tentative decision, or decision upon agency review of the decision of subordinate officers the parties shall be afforded a reasonable opportunity to submit for the consideration of the officers participating in such decisions (1) proposed findings and conclusions, or (2) exceptions to the decisions or recommended decisions of subordinate officers or to tentative agency decisions, and (3) supporting reasons for such exceptions or proposed findings or conclusions. The record shall show the ruling upon each such finding, conclusion, or exception presented. All decisions (including initial, recommended, or tentative decisions) shall become part of the record and include a statement of (1) findings and conclusions, as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the record; and (2) the appropriate rule, order, sanction, relief, or denial thereof." (5 U. S. C. § 1007(b), June 11, 1946, c. 324, § 8, 60 Stat. 242)

Section 12 Impairment of rights; effect on other laws; separability; subsequent legislation; effective date

"Nothing in this chapter shall be held to diminish the constitutional rights of any person or to limit or repeal additional requirements imposed by statute or otherwise recognized by law. Except as otherwise required by law, all requirements or privileges relating to evidence or procedure shall apply equally to agencies and persons. If any provision of this chapter or the application thereof is held invalid, the remainder of this chapter or other applications of such provision

shall not be affected. Every agency is granted all authority necessary to comply with the requirements of this chapter through the issuance of rules or otherwise. No subsequent legislation shall be held to supersede or modify the provisions of this chapter except to the extent that such legislation shall do so expressly. This chapter shall take effect three months after its approval except that sections 1006 and 1007 of this title shall take effect six months after such approval, the requirement of the selection of examiners pursuant to section 1010 of this title shall not become effective until one year after such approval, and no procedural requirement shall be mandatory as to any agency proceeding initiated prior to the effective date of such requirement." (5 U. S. C. § 1011; June 11, 1946, c. 324, § 12, 60 Stat. 244)

SUPREME COURT, U. S.

Office-Supreme Court, U.S.
FILED

JAN 9 1962

JOHN F. DAVIS, CLERK

IN THE
Supreme Court of the United States

OCTOBER TERM, 1962

No. ~~145~~ 145

FEDERAL POWER COMMISSION, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY, *Respondents*.

No. ~~50~~ 50

CITY OF PITTSBURGH, PENNSYLVANIA, *Petitioner*.

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY, *Respondents*.

On Petition for a Writ of Certiorari to the United States Court
of Appeals for the Fifth Circuit

**BRIEF OF TENNESSEE GAS TRANSMISSION
COMPANY IN OPPOSITION**

HARRY S. LITTMAN

*Attorney for Tennessee Gas
Transmission Company*

WILLIAM C. BRADEN, JR.
402 Solar Building
Washington 6, D. C.

HARRY S. LITTMAN

JACK WERNER

HAROLD L. TALISMAN

317 Wyatt Building
Washington 5, D. C.

*Attorneys for Tennessee Gas
Transmission Company*

INDEX

	Page
Opinion Below	1
Jurisdiction	2
Questions Presented	2
Statute Involved	2
Statement of the Case	3
Argument	8
Conclusion	24
Appendix A	25

CITATIONS

CASES:

<i>Atlantic Seaboard Corporation</i> , 11 F.P.C. 43 (1952) ..	11
<i>Cities Service Gas Company</i> , Docket No. RP62-1, Order issued November 1, 1961	12
<i>Colorado Interstate Gas Company v. F.P.C.</i> , 142 F. 2d 943 (10 Cir. 1944)	9
<i>Colorado Interstate Gas Company v. F.P.C.</i> , 324 U.S. 581 (1945)	23
<i>El Paso Natural Gas Co.</i> , Docket No. G-4769, Order issued December 27, 1961	22
<i>Federal Power Commission v. Natural Gas Pipeline Co.</i> , 315 U.S. 575 (1942)	12, 14, 15
<i>Natural Gas Pipeline Co. v. F.P.C.</i> , 120 F. 2d 625 (7 Cir. 1941)	15
<i>Northern Natural Gas Company</i> , 11 F.P.C. 278 (1952) ..	14
<i>Northern Natural Gas Company</i> , 11 F.P.C. 1324 (1952) ..	14
<i>Panhandle Eastern Pipe Line Company v. F.P.C.</i> , 236 F. 2d 606 (3 Cir. 1956)	12, 14, 23
<i>Phillips Petroleum Co.</i> , 24 F.P.C. 537 (1960)	13
<i>State Corporation Commission of Kansas v. F.P.C.</i> , 206 F. 2d 690 (8 Cir. 1953)	12, 13
<i>Tennessee Gas Transmission Company</i> , Docket G-525, Order issued September 20, 1956	15

	Page
<i>Tennessee Gas Transmission Company</i> , 18 F.R.C. 428 (1957)	6
<i>Tennessee Gas Transmission Company</i> , Docket No. G-11980, Order issued April 30, 1959	5
<i>Tennessee Gas Transmission Company</i> , 24 F.P.C. 204 (1960)	2
<i>Tennessee Gas Transmission Company</i> , 24 F.P.C. 525 (1960)	2
<i>Tennessee Gas Transmission Company v. F.P.C.</i> , 293 F. 2d 761, (5 Cir. 1961)	1
<i>Tennessee Gas Transmission Company v. F.P.C.</i> , 283 F. 2d 729 (5 Cir. 1960)	8
<i>United Gas Pipe Line Co. v. Mobile Gas Service Corp.</i> , 350 U.S. 333, (1956)	9, 17

STATUTES:

Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821, as amended, 15 U.S.C. 717-717w.

Section 4, 15 U.S.C. 717c	2, 4, 8
Section 5(a), 15 U.S.C. 717d(a)	8, 14

MISCELLANEOUS:

<i>F.P.C. Statistics of Natural Gas Company</i> , (1959), p. XII	7
--	---

IN THE
Supreme Court of the United States

OCTOBER TERM, 1961

No. 591

FEDERAL POWER COMMISSION,

Petitioner,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY,

Respondents.

No. 605

CITY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

**BRIEF OF TENNESSEE GAS TRANSMISSION
COMPANY IN OPPOSITION**

OPINION BELOW

The opinions of the Court of Appeals for the Fifth Circuit are reported at 293 F. 2d 761, and printed as Appendix A of the petition in No. 591. The orders

of the Federal Power Commission (R. 524-540, 585-591) ¹ are reported at 24 F.P.C. 204 and 525.

JURISDICTION

The jurisdictional requisites are adequately set forth in the petitions.

QUESTIONS PRESENTED

(1) Does the Federal Power Commission have authority under Section 4 of the Natural Gas Act to set aside filed individual zone rates, order reductions in rates and refunds prior to a determination of the zone allocation issue which is an inseparable part of determining whether the filed individual zone rates are just and reasonable?

(2) Where the issue of zone allocation has been thoroughly tried and briefed and is awaiting decision, did the Commission abuse its discretion in failing to decide that issue prior to ordering an interim reduction in rates where such action could in fact deprive Tennessee Gas Transmission Company of earning the rate of return prescribed by the Commission's interim order?

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717-717w, are set out in Appendix B to the petition in No. 591.

¹The record references "R" are to the pages of the Joint Appendix.

STATEMENT OF THE CASE

This proceeding involves a rate order of the Federal Power Commission, issued August 9, 1960, which required Tennessee Gas Transmission Company (Tennessee) to reduce its rates on an interim basis and make refunds, prior to the resolution of interrelated allocation questions necessary to a determination of which of the zone rates filed by Tennessee were unlawful. Tennessee sought to have the Commission decide the interrelated allocation questions so that it could determine from the Commission's order, which particular rates, if any, should be reduced and to whom refunds were due. The Commission denied Tennessee's request, holding that it had authority to order an interim rate reduction even though it might later find that certain rates in particular zones, which Tennessee was required to reduce on an interim basis, were in fact lawful in the first instance and that Tennessee made refunds, pursuant to the interim order, in the wrong amounts to the wrong persons.

The Court of Appeals for the Fifth Circuit affirmed the Commission's substantive determination of rate of return, but held that the Commission erred in ordering an interim reduction in rates prior to a determination of the allocation issues.

Tennessee owns and operates a natural gas pipeline system extending in a northeasterly direction from its sources of supply in Texas and Louisiana through the States of Texas, Louisiana, Arkansas, Mississippi, Alabama, Tennessee, Kentucky, West Virginia, Ohio, Pennsylvania, New Jersey, New York, Massachusetts, New Hampshire, Rhode Island and Connecticut. The rates charged by Tennessee for the transportation and sales for resale of natural gas in interstate commerce

are subject to the jurisdiction of the Commission under the Natural Gas Act (15 U.S.C. 717-717w): The Tennessee system is divided into six rate zones, with rates differing among the zones to give effect to distance from source of gas supply as well as other factors.

On October 5, 1959, Tennessee filed with the Commission, pursuant to Section 4(d) of the Natural Gas Act, schedules of rate changes designed to recover the increased cost of providing natural gas service (R. 502-504). Among the increased costs sought to be recovered was the increased interest cost on debt incurred in financing expansions of pipeline capacity approved by the Commission. Since interest costs on long-term debt constitute an integral part of the over-all return, Tennessee sought an increase in the rate of return on its investment to 7 percent solely to recover the increased cost of debt. No increase in return to the common stockholders was requested.

The rate schedules filed by Tennessee set forth the respective rates proposed by Tennessee for each class of service in each of the six rate zones on the Tennessee system.

By order issued November 4, 1959, the Commission ordered a hearing to determine the "lawfulness" of the rates which had been filed (R. 502-504). Following a five-month period of suspension, the rates became effective April 5, 1960, subject to an undertaking by Tennessee, required by Commission order, to "refund at such times and in such manner as may be required by final order of the Commission, the portion of the increased rates found by the Commission in this proceeding not justified, together with inter-

est thereon at the rate of 7 percent per annum" (R. 505-509).

Hearings commenced on February 2, 1960, and continued intermittently until recessed on May 25, 1960. During the course of the hearings, Commission Staff Counsel moved that the hearing be divided into two phases, the first phase to deal solely with the issue of rate of return, and the remaining issues to be reserved for a later stage of the proceeding. Staff Counsel further proposed that upon completion of the first phase of the proceeding, the Examiner's decision be omitted; that the Commission issue a decision determining the fair rate of return for Tennessee, and that the Commission issue an interim order requiring Tennessee to reduce its rates and make refunds, in the event the Commission should conclude that the fair rate of return is less than claimed by Tennessee (R. 377-378).

When Staff Counsel made his motion, there was pending before the Commission in the instant proceeding, and in another pending proceeding involving Tennessee (Docket No. G-11980), the issue as to the proper method of allocating Tennessee's cost of service among its six rate zones and various classes of services. Almost a year and one-half prior to the interim order in this case, the Commission had ruled that determination of the allocation issue should be expedited and, to that end, severed that issue for separate and prior hearing and determination in Docket G-11980. At the time Staff Counsel made his motion, the allocation issue had been thoroughly tried and briefed and was ripe for decision. Additionally, the

² *Tennessee Gas Transmission Company*, Docket G-11980, order issued April 30, 1959.

Examiner in the instant proceeding, who is also the Examiner in Docket G-11980, had ruled that the determination of the allocation issue in Docket G-11980 would govern the method of allocating Tennessee's cost of service in this case (R. 50-51).

Since determination of the allocation issue is required in order to translate the cost of service into rates for the various zones and services, Tennessee filed a memorandum opposing the Staff's motion for an interim order on the ground, *inter alia*, that such order would be illegal unless the Commission simultaneously determined the allocation issue (R. 591-606). On July 19, 1960, Tennessee filed a motion with the Commission requesting it to determine the allocation issue simultaneously with the issue of rate of return (R. 519-521). By order issued August 5, 1960, the Commission denied Tennessee's motion (R. 521-523).³

On August 9, 1960, the Commission issued its interim order, here involved, adopting the Staff's proposed procedure. Although the Commission found that the evidence supported Tennessee's claimed increase in cost of debt (R. 529), it disallowed Tennessee's claimed 7 percent rate of return and fixed a $6\frac{1}{8}$ percent rate of return by reducing the allowance on Tennessee's common equity some 26 percent below that which it had allowed as reasonable in a 1957 rate decision.⁴ The Commission's order required Tennessee

³ Petitioner in No. 591 (p. 5) alleges that the motion filed by Tennessee was untimely, but fails to mention the fact that it was not denied on that ground.

⁴ In *Tennessee Gas Transmission Company*, 18 F.P.C. 428, 430 (1957), adopting and modifying on other grounds an Examiner's decision at 18 F.P.C. 439, 441, the Commission found that a 13.71% return on common equity was reasonable. In the instant case, the

to file reduced rates retroactively to April 5, 1960, and required Tennessee to make refunds of the differences in rates collected since April 5, 1960 (R. 524-540).

The Commission, however, failed to make any determination as to the proper method of cost allocation which should be employed in allocating the reduced over-all cost of service among the six rate zones and various classes of service on the Tennessee system. Nor did the Commission make a determination or findings as to which of the various zone rates filed by Tennessee were unlawful, which rates should lawfully be reduced, or to whom refunds were lawfully due. Instead, the Commission left these crucial questions open for later decision, even though such later decision might result in a determination that Tennessee had reduced rates in various zones, pursuant to the interim order, which were in fact lawful in the first instance and had made refunds in the wrong amounts to the wrong customers.

Since the Commission's order in effect required Tennessee's stockholders to absorb virtually the entire increase in cost of debt, by reducing the return allowance on equity below that commensurate with returns being earned by other pipelines; and since the requirement of an immediate reduction in rates prior to a determination by the Commission as to how such reduction should be allocated among the six rate zones threatened to deprive Tennessee of the opportunity of even earning the return which the Commission fixed,

Commission reduced the return on common equity to 10.12% (R. 534). This return on equity was 20% below the lowest average return on equity earned by the major pipelines in any year since 1951 (R. 475), and was below the lowest amount earned by the pipeline industry as a whole since 1951. *F.P.C. Statistics of Natural Gas Companies* (1959), p. XII.

Tennessee applied for a rehearing of the Commission's order (R. 541-576). On September 27, 1960, the Commission denied Tennessee's application for rehearing (R. 585-591).

On October 3, 1960, Tennessee filed its Petition to Review with the Fifth Circuit Court of Appeals.⁵ As stated above, by its decision issued August 2, 1961, the Court upheld the Commission's substantive determination as to rate of return, but it held that the Commission erred in requiring a reduction in rates and refunds to be made prior to a determination of the pending allocation issues, since the failure to decide the allocation issue threatened to deprive Tennessee of the return which the Commission found proper.

Petitioners in Nos. 591 and 605 contend that the Court below erred in setting aside the portion of the Commission's order dealing with the interim order. Since both petitions seek certiorari to review the same judgment, and since the basic issues raised in both cases are the same, this single brief is filed in opposition to each of the petitions.

ARGUMENT

The decision below follows the rationale of leading cases defining the Commission's authority under the rate provisions of Sections 4 and 5 of the Natural Gas Act. These cases hold that rates filed with the Commission "can be set aside *only* upon being found un-

⁵ Tennessee simultaneously filed a motion for stay of the Commission's order, which was denied, Judge Wisdom dissenting. *Tennessee Gas Transmission Company v. F.P.C.*, 283 F. 2d 729. After the denial of the stay, Tennessee reduced its rates and made refunds to its customers, subject to its right to recoupment in the event the Commission's order was overturned on appeal.

lawful by the Commission.”⁶ *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 333, 342 (1956); *Colorado Interstate Gas Co. v. F.P.C.*, 142 F. 2d 943, 954 (10th Cir. 1944), affirmed 324 U.S. 581. The Court below simply held that the same standards apply to an interim rate reduction order as apply to a final rate reduction order issued at the conclusion of the proceeding.

(1) In the case at bar the Commission found that the rates filed by Tennessee were “excessive” (R. 537). However, it had no basis for making such a finding, because a valid determination of whether or not any of the individual zone rates filed by Tennessee are “excessive” and, therefore, unlawful depends not only on a correct decision as to the rate of return, but also as to the proper method of allocating the cost of service among the various zones.

As stated above, the 17-state area in which Tennessee transports and sells natural gas is divided into six established rate zones for rate-making purposes. The aforementioned allocation issue pending before the Commission in the prior rate proceeding involving Tennessee (Docket G-11980) will, when resolved, determine for the first time the proper method of allocating Tennessee’s cost of service among the various rate zones and services for the purpose of designing rates. As stated previously, the Examiner has ruled that the determination of the allocation issue in Docket G-11980 will govern the allocation of cost of service in the case at bar.⁷

⁶ Emphasis is supplied throughout this brief unless otherwise indicated.

⁷ No appeal from this ruling was taken by any of the parties to the instant proceeding.

The diverse methods of allocation which have been submitted by the parties in the G-11980 proceeding yield such drastically different results, that even if there is a substantial reduction in the over-all cost of service claimed by Tennessee, there may be no reduction in rates in certain zones depending on the allocation method selected (R. 594-595, 598). For example, in the G-11980 proceeding the Commission's Staff claims that Tennessee's total cost of service is approximately \$185,700,000. Of this amount, Tennessee's customers in West Virginia (Eastern Zone) contended that under their method of allocation approximately \$24,000,000 should be collected from customers in the New England Zone, \$62,000,000 from the customers in West Virginia, and the balance from customers in the other four zones. Tennessee's New England customers, on the other hand, claim that New England should bear only \$16,800,000 of the cost of service and that the West Virginia customers are responsible for almost \$68,000,000 (R. 593-96, 598). Tennessee, which claims a higher cost of service than the Staff, predicated its rates on an allocation of approximately \$21,000,000 to New England and \$72,000,000 to West Virginia. Thus, West Virginia's method of allocation would allocate approximately \$3,000,000 more costs to New England than the revenues which Tennessee's filed rates yield in the New England Zone. Hence, even if the Staff's cost of service were adopted, under West Virginia's method of allocation there should be no reduction in rates in New England, since Tennessee's filed rates for that zone would not be excessive.

* The West Virginia method of allocation is sometimes referred to in the record as the "Columbia" method (R. 594-5).

The foregoing demonstrates that it is impossible, without determining the allocation issue, for the Commission to find, as required by the Act, that the specific zone rates filed by Tennessee are unlawful. Here the Commission has only determined that there should be an approximate \$11,000,000 *over-all* reduction in the aggregate level of the rates due to the reduced rate of return. However, by reason of its failure to decide the allocation issue, the Commission had no basis for determining which of the filed rates in the six zones are unlawful, the extent that the individual filed rates should be reduced, or to whom refunds were lawfully due. Although these determinations are necessary prerequisites to its action, the Commission's order required Tennessee to reduce its rates in each of the zones and make refunds to customers in each zone at the risk of a later determination by the Commission that Tennessee had reduced rates (pursuant to the interim order) which were in fact lawful in the first instance and had made refunds in the wrong amounts to the wrong customers. Under the Commission's interpretation of the Act, it would have no power retroactively to increase Tennessee's rates back to the originally filed level even though it later found certain of those rates to have been lawful.⁹ As Judge Wisdom aptly pointed out below, the Commission failed to "put the horse where he belongs—in front of the cart."¹⁰

⁹ The Commission interprets the Act as precluding it from increasing rates above those on file with the Commission. *Atlantic Seaboard Corporation*, 11 F.P.C. 43, 63-65 (1952). Since the rates filed by Tennessee were set aside by the interim order, the Commission deems those rates as no longer being on file.

¹⁰ Order issued October 28, 1960, denying motion for stay, dissent, p. 3.

(2) Petitioners contend that the decision of the Court below would outlaw the use of the so-called interim order procedure, even though that procedure was judicially approved in *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575 (1942); *Panhandle Eastern Pipe Line Co. v. Federal Power Commission*, 236 F. 2d 606 (3d Cir. 1956); and *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F. 2d 690 (8th Cir. 1953). They argue that unless this Court strikes down the portion of the Fifth Circuit's decision dealing with the interim order procedure, the Commission will lose a valuable tool "designed to carry out the mandate of Section 4 of the Natural Gas Act that the Commission decide increased rate questions as speedily as possible" (Petition No. 591, pp. 8-9).

The interim order procedure is a procedure whereby the Commission decides issues in a rate case on a piecemeal basis rather than issuing a single decision as to all issues involved. Since this procedure requires more than one decision and a series of briefs, it is highly debatable whether it does, in fact, result in deciding rate cases "as speedily as possible."¹¹ Indeed, there is growing belief that the interim order procedure retards rather than accelerates the ultimate disposition of rate cases. In point are the following observations of Commissioner Kuykendall recently made in voicing his objections to invoking the interim order procedure in *Cities Service Gas Company*, Order issued November 1, 1961 in Docket RP62-1 (dissent):

¹¹ For example, the rates here involved were filed on October 5, 1959. The interim order on rate of return was issued on August 9, 1960. The remaining issues are still pending before the Hearing Examiner.

"I concur in the result, but do not agree with all that is said. I have always had some reservations about the worth of the interim order procedure, but was willing to give it a thorough trial. Our experience has convinced me that its faults outweigh its virtues.

"I now am confident that our rate cases can be handled more expeditiously if we concentrate on complete conclusion of them, rather than taking piece meal action. Furthermore, it is obvious that we are compounding the already excessive amount of litigation which ensues from our decisions."

Contrary to the implication in the petitions, the procedure has not been widely used in the past. In fact, prior to the time the rates here involved were filed, the Commission had invoked this procedure only three times, that we know of, in over 20 years of regulation under the Natural Gas Act.¹³

¹² It is pertinent to note that in the instant Tennessee case, Commissioner Kuykendall supported the interim order procedure, dissenting only as to the rate of return allowed. (R. 540).

¹³ The interim order procedure has not been used in any case involving rate increases filed by independent producers, notwithstanding the fact that such cases constitute the great bulk of the Commission's backlog of pending cases and were the primary cause for the filing of rate increases by the pipeline companies which purchase gas from such producers. In *Phillips Petroleum Co.*, Opinion 338 (issued September 28, 1960) 24 F.P.C. 537 at 545, 546, the Commission stated that:

"* * * Currently, 570 of these producers are involved in 3,278 producer rate increase filings now under suspension and awaiting hearings and decisions. The number of completions of independent producer rate cases per man-year during the first 6 years following the Phillips decision indicate that nearly 13 years would be required for our present staff to dispose of the 2,313 cases pending on July 1, 1960. Within this 13-year period an additional estimated 6,500 cases would have been received."

In the three previous cases, *supra*, where such procedure has been applied, however, the Commission could and did find that the rates filed were unlawful upon the basis of the interim issues decided. As Commission Counsel conceded on oral argument in the Court below,¹⁴ none of those cases, which are the same three cases now relied on by Petitioners, had pending rate design and allocation issues which could be applied retroactively to change the results of the interim order. Hence, unlike the instant case, the basis upon which interim rates were reduced and refunds were made was final and could not be adjusted retroactively.¹⁵

¹⁴ This concession was made at the oral argument on October 19, 1960 (Tr. 36) before the Court below on the motion for stay. The oral argument was transcribed with the Court's permission.

¹⁵ In the *Panhandle* case, *supra*, the Commission, just 75 days prior to the interim order, had decided rate design and allocation issues for the Panhandle system. The interim order made it clear that it would not retry these issues and that the interim reduction in rates should be based on the same allocation method just decided (See 236 F. 2d at p. 611). Thus, as the Court pointed out in the *Panhandle* case the issues decided on an interim basis were "severable" from the remaining issues in that case (236 F. 2d at 608). The *State Corporation Commission* case, *supra*, which involved an interim reduction in rates for Northern Natural Gas Company, is inapposite because there were no jurisdictional rate zones on the Northern system at the time of the interim order. Since Northern had single system-wide rates, no allocation to zones was necessary. While there was an issue pending as to allocation of costs between jurisdictional and non-jurisdictional gas business, the Commission dismissed that issue in its interim order because a method of allocation had just been prescribed in a previous opinion. Thus, for purposes of allocating costs between jurisdictional and non-jurisdictional business, the Commission adopted the allocation method that had just been prescribed. See *Northern Natural Gas Company*, 11 F.P.C. 278 and 11 F.P.C. 1324 (1952). Since the *Natural Gas Pipeline* case, *supra*, was a Section 5(a) investigation, it is clearly inapposite because under Section 5(a) of the Act the Commission's orders have prospective effect only. Thus, if the Commission had adopted a different method of allocation subse-

Whether or not the interim order procedure is a desirable means of expediting rate cases is really beside the point, for the Court below does not hold that the Commission lacks authority to utilize this procedure. It holds, instead, that in the special circumstances of *this case* it was unlawful and an abuse of discretion for the Commission to order an interim reduction in rates prior to a determination of the pending allocation issue. In so doing, the Court relied on the Commission's own decision in an earlier Tennessee rate case involving similar circumstances where the Commission itself refused to adopt the interim order procedure on the ground that it would be "premature," "unfair" and "improper" to issue an interim order before determining the pending allocation issue. The following reasons given by the Commission in its earlier decision for refusing to fix interim rates prior to a determination of the pending allocation issue provide powerful support for the decision of the Court below:¹⁶

"The pleadings pose the questions of whether it is appropriate and in the public interest for the Commission *at this time and on the present record* to consider and determine separately the issues relating to total cost of service and rate level and to reserve for subsequent decision the issue raised

quent to the interim order, it could not have been applied retroactively. For this reason, as the Court of Appeals noted in the *Natural Gas Pipeline* case, the interim order procedure could in no way injure the pipeline company in that case (120 F.2d 625, 631). It is significant to point out that although Judge Tuttle dissented below, he did not claim that the majority decision was in conflict with the above cases.

¹⁶ *Tennessee Gas Transmission Company*, Docket G-5259, Order issued September 20, 1956, mimeo. pp. 3, 5, 6. Tennessee took the position in that case that the cost of service issues could be separated from the allocation issues if the Commission, upon deciding the allocation issue would apply it *prospectively only*.

concerning zone rate differentials; and should the intermediate decision procedure be omitted.

* * * * *
 " * * * * Since Tennessee is engaged in rendering jurisdictional and non-jurisdictional service, it is not possible to translate the 'total' of Tennessee's cost of service into jurisdictional 'rate level' without first determining the portion of the 'total' properly allocable to jurisdictional sales. Accordingly, even though we find that it is now appropriate to determine the 'total' of Tennessee's cost of service, such cost of service cannot be translated into jurisdictional rates (or 'rate level') until decision is made as to the proper method of allocating the 'total' between jurisdictional and non-jurisdictional sales.

"Fulfillment of the request of Tennessee that determination be now made as to its total cost of service and the rate level would not only require determination as to the proper method of allocating the 'total' between jurisdictional and non-jurisdictional sales, but it would require also present determination as to the proper method of allocating the jurisdictional portion of the 'total' between the several zones of service, or, at least, a determination that the present zone boundaries and rate differentials should be maintained for sales made on and since December 15, 1954, and continuing until final order in this proceeding. It is not possible at this incomplete state of the proceeding to determine proper zone boundaries and what method of allocating costs between zones would be fair and equitable.

* * * * *
 " * * * * our experience tells us that, if *in the future* a change in Tennessee's zone boundaries or rate differentials is in order, the effect of the resultant rate on particular customers will differ dependent upon what cost of service is found

proper here. On this record, however, it is not possible to now determine what the effect upon particular customers will be until resolution of the cost of service and zone issues.

"Thus, we are of the opinion that it would be not only premature for us to grant that part of Tennessee's motion requesting that we at this time fix rates to be effective on and after December 15, 1954, it would also be *unfair and improper*."

As the Commission recognized above, it cannot separate what is inextricably joined together. In order to determine which of Tennessee's zone rates are excessive and, therefore, unlawful as a result of the interim issue decided, the Commission, admittedly, must determine the allocation issue. In setting aside rates which it may later find lawful, the Commission clearly exceeded its authority under the Act, for, as pointed out above, this Court has held that, rates filed with the Commission "can be set aside *only* upon being found unlawful by the Commission." *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 333, 342 (1956).

(3) While the Commission concedes that its failure to determine the allocation issue may result in Tennessee not being able to earn the return which the Commission found proper, it claims that Tennessee cannot be heard to complain because Tennessee has the burden of justifying its rates on the basis of its own presentation (Petition, pp. 15-16). To be sure, Tennessee does have the burden of proof. But we fail to understand—nor did the Court below—how the Commission can validly argue that Tennessee cannot be heard to complain about an order which determines that consumers are entitled to an approximate \$11,000,000 reduction in

rates as a result of the rate of return determination, but it establishes a procedure which may require Tennessee to reduce its rates by *more* than \$11,000,000.

The undertaking filed by Tennessee and prescribed by the Commission, when the originally filed rates here involved became effective, was that Tennessee would "refund at such times and in such manner as may be required by final order of the Commission, *the portion of the increased rates found by the Commission in this proceeding not justified*, together with interest thereon at the rate of 7 percent per annum" (R. 507-509). Neither the Act nor Tennessee's refund obligation entitled the consumer to reduced rates or refunds in excess of the portion of Tennessee's rates found not lawfully justified, and the Commission has no authority to require Tennessee to reduce its rates or make refunds until it properly determines which of Tennessee's respective zone rates is in fact not lawfully justified.

(4) The Commission contends, however, that the possibility of Tennessee being harmed by the interim order is remote because (1) the presiding examiner has concluded in his recommended decision that Tennessee's allocation method should be adopted by the Commission without substantial modification; and (2) the Commission's staff is advocating in the second phase of the reserved hearing a total cost of service about \$36,000,000 less than that contended for by Tennessee¹⁷ (Petition, p. 15, fn. 14). Such contentions are obviously lacking in substance because they are based upon speculation as to the future outcome of these

¹⁷ There is nothing in the record which supports Pittsburgh's assertion that past experience (based on rate cases concluded in fiscal 1961) indicates that "a substantial portion of the total increases will be found unjustified" (Pittsburgh's petition, p. 11).

undecided issues. Any conclusion at this time that Tennessee will not be harmed by the interim order necessarily involves a prejudgment of the Commission's final decision of these undecided matters.

At best, such contentions amount to nothing more than an observation that this proceeding may become moot if the Commission should agree with the Examiner's recommended decision on the allocation issue, assuming, of course, that no appeal is taken from the Commission's decision by parties other than Tennessee.

(5) The petitions of the Commission (pp. 10-12, 17-20) and the City of Pittsburgh (pp. 9-12) attempt to justify the interim order on the grounds of expediency. They argue that unless the Commission can set aside rates on an interim basis prior to a determination of their lawfulness, it will delay refunds to consumers. But such contention begs the fundamental question of whether the interim order is lawful under the special facts and circumstances of this case. No one questions the desirability of expediting hearings and decisions of rate proceedings before the Commission. Here, however, the Commission, in its haste to get partial refunds into the hands of Tennessee's customers, failed to decide the all-important allocation issue, and thereby failed to make the required findings as to which particular rates in the individual zones were unlawful. It, therefore, failed to determine what refunds were *lawfully* due to which customers in the various zones, thereby jeopardizing Tennessee's ability to recover the very return which the Commission found proper. For Tennessee cannot recoup (through retroactive rate increases) refunds required by the interim order to be made to customers which the Commission may later

find, when it finally decides the allocation issue, were not entitled to such refunds.

The Commission's interim order procedure thus presents a case of "haste making waste"—a situation which could have been readily avoided by simply deciding the allocation issue (then ripe for decision) simultaneously with the rate of return issue.¹⁸

Additionally, the assertion by the Commission (Petition, p. 11) that pipelines gain by the delay in disposition of refund money because they provide a cheap source of expansion capital is completely without substance and is a gross misconception of financial fact. Apart from the fact that there is no support for the assertion that pipelines deliberately file "excessive" rates, the Commission erroneously states that the 7 percent interest which it requires pipelines to pay on refunds is not an effective deterrent to "excessive" rate filings, because the interest is tax deductible. Thus, the Commission argues, the effective cost to the pipeline is approximately one-half the 7 percent interest rate. The fact is, however, that the cost to the pipeline before taxes is more than 14 percent and after the tax deduction it is 7 percent.

Money collected subject to refund is used (1) to pay operating expenses, (2) to provide additional income to which the pipeline company feels it is en-

¹⁸ The implication in the petitions that great harm would have been caused to consumers by delaying a reduction in rates until disposition of the allocation issue is without merit. The approximate \$11,000,000 reduction in rates ordered by the Commission would result in a savings of less than 15¢ per month to the typical householder. See, Reply of Tennessee Gas Transmission Company to Opposition of the Federal Power Commission to Motion for Stay, pp. 2-3, submitted below in Case No. 18547 on October 14, 1960.

titled, or (3) both. To the extent such money, or any part of it, is required to pay operating expenses, it is obviously not available for expansion purposes.

To the extent it provides additional income, such amount is taxable at the full corporate rate and 52 cents of each dollar is promptly paid to the government as federal income taxes, leaving only 48 cents of each dollar available to the company for expansion or other company purposes.

This result is ignored by the Commission in asserting (Petition, p. 11) that the pipelines' obligation to pay interest on refunds cannot be regarded as an effective deterrent to "excessive" rate filings. The required payment of 7 percent interest on each dollar received in order to have 48 cents available for expansion results in an effective interest cost of 14.5833 percent. Concurrently, Tennessee had bank notes outstanding on which it paid 4.375 per cent interest (R. 486). The entire principal amount borrowed on such bank notes is available for expansion or other company purposes.

The comparison of this 4.375 percent interest rate with the 14.5833 percent rate, resulting from 7 percent interest on refunds, demonstrates the harsh effectiveness of the deterrent. It is true that interest paid is deductible for income tax purposes; however, application of the 52 percent tax rate merely reduces the 14.5833 percent interest rate to 7 percent net effect after taxes. By the same token, the 4.375 percent interest on bank notes is reduced to 2.2728 percent net after taxes. Thus, the tax deduction does not alter the comparison nor the effectiveness of the deterrent. Hence, the contention that pipelines file "excessive"

rates to obtain a cheap source of expansion capital is without any foundation in fact or reason.¹⁹

(6) Although the Commission concedes that the Court's decision "emphasizes" the special circumstances present in this case, it argues that the decision "appears to have wide application" (Petition, p. 17). But the Commission has experienced no difficulty in applying the interim order procedure since the issuance of the Court's decision in this case. Recently, the Commission granted a motion by its Staff to invoke the interim order procedure in a rate proceeding involving El Paso Natural Gas Company, wherein the Staff urged that:²⁰

"* * * the *Tennessee* decision (*Tennessee Gas Transmission Company v. F.P.C.*, 293 F. 2d 761) is distinguishable from these proceedings in that here there are no other issues ripe for decision whereas in *Tennessee* the basis of the court's refusal to allow the interim order to become effective was the fact that the allocation issue was ripe for decision; * * *."

As we read the Court's decision, it would only prevent the Commission from ordering an interim reduction in rates when it has not determined those issues necessary to a finding that the rates filed are in fact unlawful. Contrary to the Commission's assertions, allocation of costs among zones is not an issue in "virtually every major pipeline case." Only a few of the rate cases decided by the Commission in more than

¹⁹ There is no reason why pipelines should be deterred from filing needed increases in rates. The proper purpose of the interest charge on refunds is to compensate the consumers, not to penalize pipelines for having filed a rate increase.

²⁰ *El Paso Natural Gas Co.*, Docket No. G-4769, *et al.*, order issued December 27, 1961. For the convenience of the Court, a copy of said order is attached hereto as Appendix A.

twenty years have involved this issue and once the Commission decides the issue, it has held that it will not retry it in another case unless there has been a substantial change in circumstances.²¹

Indeed, since the Commission has issued no rules nor prescribed any general method with regard to zone allocation, and since the few previous Commission decisions involving this issue have applied widely different methods, it is virtually impossible for a pipeline to predict what zone allocation method the Commission will adopt for rate-making purposes. By requiring Tennessee to guess, at its peril, what allocation method the Commission will later adopt, the Commission would relegate rate filings into a "poker game" in which only the pipeline could be the loser.²² The Court below holds that it was unfair and improper for the Commission to adopt such a procedure in a case such as this, when it could result in Tennessee being deprived of revenues needed to meet the cost of providing a valuable service upon which the public depends. It was particularly unfair here because the Commission could have readily resolved the problem by deciding the allocation issue which was ripe for decision.²³

²¹ For example, as pointed out above, in this very case the Examiner has ruled that the decision as to allocation in Docket G-11980 will apply to the instant case. Also see, *Panhandle Eastern Pipe Line Company v. F.P.C.*, *supra*, where the Commission refused to retry the allocation issue because there had been no substantial change in circumstances.

²² As this Court has aptly observed, allocation of costs "is not a matter for the slide rule," but instead "involves judgment on a myriad of facts." *Colorado Interstate Gas Co. v. F.P.C.*, 324 U.S. 581, 589 (1945).

²³ The Commission argues (Petition, p. 16) that since the allocation issue was complex, the Commission properly denied Tennessee's request to omit the intermediate decision on allocation so

In summary, the petitions should be denied not only because the decision below is correct, but also because it does not conflict with any previous decisions, and is admittedly based on the peculiar facts and circumstances connected with this case, and, therefore, is not likely to have broad applicability.

CONCLUSION

In view of the foregoing, we respectfully urge that the Petitions for Certiorari be denied.

Respectfully submitted,

HARRY S. LITTMAN

Attorney for Tennessee Gas Transmission Company

WILLIAM C. BRADEN, JR.

402 Solar Building
Washington 6, D. C.

HARRY S. LITTMAN

JACK WERNER

HAROLD L. TALISMAN

317 Wyatt Building
Washington 5, D. C.

*Attorneys for Tennessee Gas
Transmission Company*

January 9, 1962

that it could be decided simultaneously with the rate of return issue. But the Court below does not hold that the Commission erred by not omitting the intermediate decision on allocation. It holds that the Commission erred in ordering a reduction in rates prior to a decision on allocation. Moreover, it should be noted that the record on rate of return was also complex, but the Commission omitted the intermediate decision on that issue (R. 513-516).

APPENDIX A

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Before Commissioners: Joseph C. Swidler, Chairman;
Jerome K. Kuykendall, Howard Morgan, L. J. O'Connor,
Jr., and Charles R. Ross.

Docket Nos. G-4769, G-12948, G-17929 and RP60-3
EL PASO NATURAL GAS COMPANY

**Order Adopting Interim Order Procedure Omitting Intermediate
Decision and Fixing Dates for Filing of Briefs**

(Issued December 27, 1961)

The Presiding Examiner, on November 30, 1961, certified to the Commission the record made in these dockets since July 24, 1961 relevant and material to the issue of rate of return, and a motion entered orally upon the record by staff counsel during the hearing on November 16, 1961. In that motion staff counsel requested (1) application in these proceedings of the interim order procedure with respect to the issue of rate of return, and (2) waiver of the intermediate decision procedure in accordance with Section 1.30 of the Commission's Rules of Practice and Procedure and immediate certification of the issue of rate of return, with the testimony and exhibits related thereto, to the Commission for decision on that issue. Several interveners supported the motion while El Paso objected to it both on the record and by written answer filed November 27, 1961.

It is contemplated that El Paso will be required to reduce its present rates if it is determined under the interim order procedure that the fair rate of return for El Paso is less than that requested in RP60-3. If the fair rate of return is less than that requested in Docket Nos. G-4769, G-12948 and G-17929, it is contemplated that immediate refunds would be ordered in only Docket No. G-4769, for reasons hereinafter stated. Refunds, if necessary, in Docket Nos.

G-12948, G-17929 and RP60-3, would not be ordered until determination of all the issues in those proceedings. It is further contemplated that for purposes of refund and reduced rates, all other factors relating to rate base, cost of service, allocation, etc., will be used as presented by El Paso on the record, without prejudice to the rights of any party to question any of those items in subsequent phases of this proceeding, if such item is determined to be in issue by the Presiding Examiner.

Staff counsel asserts that the interim order procedure is necessary and proper in these proceedings, will expedite these proceedings and will result in substantial justice to El Paso and its customers. In support of his motion staff counsel contends: (1) As the only issue in Docket No. G-4769 is that of a fair return on El Paso's production properties, pursuant to the remand by the Fifth Circuit Court of Appeals, 281 F. 2d 567, the granting of the motion would dispose of that case finally; (2) the Commission, in considering the rate of return issue for the purpose of finally deciding G-4769, will necessarily be reviewing the identical record which relates to the rate of return issue in the latter three dockets; (3) a prompt decision on rate of return could give immediate relief to all of El Paso's customers, particularly those in California which take the bulk of El Paso's gas; (4) the *Tennessee* decision (*Tennessee Gas Transmission Company v. F.P.C.*, 293 F. 2d 761) is distinguishable from these proceedings in that here there are no other issues ripe for decision whereas in *Tennessee* the basis of the court's refusal to allow the interim order to become effective was the fact that the allocation issue was ripe for decision; and (5) if the Commission should find that a lesser rate of return is just and reasonable, than that requested by El Paso in Docket Nos. G-12948, G-17929 and RP60-3, it is suggested that a deferral of refunds until final decision of all issues in those proceedings would enable El Paso to earn the rate of return finally determined by the Commission even if the Commission in

its final decision, should change El Paso's allocation method.

El Paso, in its answer to staff counsel's motion, in addition to prematurely arguing the merits of its evidence on rate of return, also contends and argues that: (1) to grant such a motion under the circumstances of this case would be unlawful; (2) even if it were not unlawful, to grant a motion for interim order in this case would be unfair, unwise and not in the public interest; (3) the Presiding Examiner does not have power to grant a motion for interim order procedure in these cases and (4) the motion for omission of the intermediate decision should be denied, because to grant such a motion in this case would be unlawful and even if it could lawfully be done, intermediate decision should not be omitted here.

The Presiding Examiner, in his ruling of November 30, 1961, on staff counsel's motion, granted staff's request for certification of the record on the issue of rate of return. The Examiner found that the waiver of the intermediate decision procedure, and the use of the interim order procedure (pursuant to the Commission's order of November 1, 1961, in *Cities Service Gas Company*, Docket No. RP62-1) will expedite these proceedings and, "with the reservations and conditions proposed by the staff, modified, if the Commission should find that necessary or desirable, be just to all of the parties to these proceedings." The Presiding Examiner then certified the record relating to the rate of return issue to the Commission, as requested in the staff's motion.

El Paso, on December 5, 1961, filed its "Appeal by El Paso Natural Gas Company from Presiding Examiner's Ruling On Motion to Certify; Motion Requesting Opportunity to File Briefs; and Motion Requesting Opportunity to Present Oral Argument." El Paso repeats therein the arguments contained in its answer to staff's motion. El Paso also contends that the Presiding Examiner's final

ings in his ruling on staff counsel's motion were not made through the exercise of any discretion conferred upon him by the Rules but because the Examiner considers himself bound by the Commission's order of November 1, 1961 in Docket No. RP62-1, "as committing to him for initial decision only the question 'whether the use of the procedure [interim order] will expedite this proceeding and be just to the parties . . . ' ". El Paso alleges that the Examiner's finding decides only part of the issues relating to the interim order procedure and that such a method, as set out by the Commission in its *Cities Service* order would, "to no good purpose, fragment the decision-making process and prevent any benefit from being derived from initial decision by the Examiner." For these reasons, El Paso requests the Commission to remand these proceedings to the Examiner for his decision on the question of the propriety of the use of the interim order procedure in these proceedings, taking into account "all" of the factors which bear on that problem. However, El Paso fails to point to any factors (other than those covered by the Presiding Examiner in his certification) which it believes relate to the propriety of the use of the interim order procedure. Further, we cannot agree with El Paso's contention that the Presiding Examiner's finding that the procedures proposed by the staff "would expedite the disposition of the proceedings" and "would be just to all of the parties to the proceeding" was based on less than "all" the factors bearing on the problem.

The Commission finds:

(1) The use of the interim order procedure with respect to the rate of return issue in these proceedings is both necessary and proper and will expedite these proceedings and result in substantial justice to all parties.

(2) The staff's motion for application of the interim order procedure and waiver of the intermediate decision with respect to the rate of return issue should be granted

and the parties should be allowed to file briefs as hereinafter provided.

(3) El Paso's "Appeal From Presiding Examiner's Ruling on Motion To Certify; Motion Requesting Opportunity To File Briefs; And Motion Requesting Opportunity To Present Oral Argument" should be denied.

The Commission orders:

(A) The issue of a proper rate of return for El Paso in these proceedings shall be determined under interim order procedure.

(B) The intermediate decision procedure hereby is omitted for purposes of determination of the proper rate of return for El Paso.

(C) El Paso's "Appeal From Presiding Examiner's Ruling On Motion To Certify; Motion Requesting Opportunity To File Briefs; And Motion Requesting Opportunity To Present Oral Argument" hereby is denied.

(D) Main briefs on the issue specified in Paragraph (A) above shall be filed by all parties who desire to do so on or before January 22, 1962, and reply briefs, if any, shall be filed on or before February 2, 1962.

By the Commission. Commissioner Kuykendall dissenting.

J. H. GUTRIDE,

Joseph H. Gutride,

Secretary.

In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 591

FEDERAL POWER COMMISSION, PETITIONER

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, AND UNITED FUEL GAS COMPANY

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM IN REPLY TO RESPONDENTS' BRIEFS IN OPPOSITION

This reply is for the sole purpose of restating and amplifying our view (Pet. 11) that a pipeline's obligation to pay interest on refunds cannot be regarded as an effective deterrent to excessive rate filings. Both Tennessee (Brief in Opp., pp. 19-22) and Manufacturers (Brief in Opp., pp. 13-14) argue that if such funds are used for capital expansion the effective interest rate on such capital is approximately 14 percent before taxes for a corporation in the 52 per-

(1)

cent tax bracket.¹ But, as Tennessee correctly states (Br. in Opp., p. 21), the interest rate after taxes on that portion of excess rate available for use as capital is approximately 7 percent. However, Tennessee is not correct in its conclusion that this 7 percent interest rate acts as a deterrent to filing for excessive increases because borrowing from other sources can be done at lower rates. The 7 percent cost of such capital is not properly to be compared with the cost of debt capital, since capital thus raised from the ratepayers can be treated as equity by the pipelines. The proper comparison is with the cost of equity money, which is in the neighborhood of 10 percent or more.² Moreover, by making the ratepayers provide equity capital, the common stockholders, trading on this equity, are enabled to obtain additional senior capital at less than the overall return earned by the company. The difference between the cost of senior capital and the overall return is, of course, income which increases the earnings per share of common stock. These earnings per share will, it is also clear, increase more rapidly if the number of shares of common stock entitled to the equity earnings remains

¹ It should be pointed out that on a corporation's current year's taxes there is a six-month's payment lag. The corporation has the free use, for a period equal to the period of collection of excessive rates, of approximately one half of a year's taxes, which materially reduces the 14% figure used by respondents.

² The 7% and 10% figures here compared correspond to 3 1/2% (see Petition, p. 12) and 5%, respectively, on the gross excess collected from the ratepayers.*

constant, instead of being increased by the issuance of new stock, while the plant and earnings are expanded.

Unwarranted rate increases make consumers involuntary lenders. We believe that the interim order is an important tool—one which should be used more, rather than less, frequently—in providing relief from this burden.

For the reasons stated in the petition and in this reply memorandum, we respectfully submit that the petition for a writ of certiorari should be granted.

ARCHIBALD COX,
Solicitor General.

RALPH S. SPRITZER,
General Counsel,
Federal Power Commission.

JANUARY 1962.

In The
Supreme Court of the United States

No. 48
October Term, 1962

FEDERAL POWER COMMISSION, Petitioner

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE
MANUFACTURERS LIGHT AND HEAT COMPANY, THE
OHIO FUEL GAS COMPANY AND UNITED FUEL GAS
COMPANY

No. 50
October Term, 1962

CITY OF PITTSBURGH, PENNSYLVANIA, Petitioner.

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE
MANUFACTURERS LIGHT AND HEAT COMPANY, THE
OHIO FUEL GAS COMPANY AND UNITED FUEL GAS
COMPANY

On Writ of Certiorari to the United States Court of Appeals
for the Fifth Circuit.

**BRIEF AMICUS CURIAE OF THE COMMONWEALTH OF
PENNSYLVANIA AND THE PENNSYLVANIA PUBLIC
UTILITY COMMISSION IN SUPPORT OF THE FEDERAL
POWER COMMISSION**

HERBERT E. SQUIRES

Assistant Counsel

ALAN R. SQUIRES

Assistant Counsel

JOSEPH I. LEWIS

Counsel

**For the Pennsylvania Public
Utility Commission**

DAVID STAHL

Attorney General

Commonwealth of Pennsylvania

North Office Building
Harrisburg, Pennsylvania

INDEX

	PAGE
Interest of Amicus Curiae	1
Statement of the Case	3
Argument:	
A. The Importance of and Necessity for the Interim Order Procedure in Rate Proceed- ings	4
B. The Lower Court's Error	11
Conclusion	16

TABLE OF CITATIONS

CASES:

Atlantic Refining Co. v. Public Service Commis- sion of New York, 360 U.S. 378	5
Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591	8
Federal Power Commission v. Natural Gas Pipe- line Co., 315 U.S. 555	13, 14, 15
Los Angeles Gas Corp. v. Railroad Commission, 289 U.S. 287	13
Natural Gas Pipeline Co. v. Federal Power Com- mission, 120 F. 2d 625 (C.A. 7)	6
Panhandle Eastern Pipeline Co. v. Federal Pow- er Commission, 143 F. 2d 488 (C.A. 8)	13

STATUTES:

**Natural Gas Act, June 21, 1938, c.556, 52 Stat.
821-833, as Amended, 15 U.S.C. 717-717w:**

Section 4, 15 U.S.C. 717e 4

Section 4(e), 15 U.S.C. 717e(e) 4, 5, 8, 10

Section 5(a), 15 U.S.C. 717d(a) 12

**Public Utility Law, Act of May 28, 1937, P.L.
1053, 66 Purdon's Penna. Statutes An-
notated 1101 1**

4 INTEREST OF AMICUS CURIAE

The Commonwealth of Pennsylvania and the Pennsylvania Public Utility Commission, an agency of the Commonwealth, file this Brief pursuant to Rule 42(4) of the rules of this Court.

The Pennsylvania Public Utility Commission respectfully represents that it is a regulatory body of the Commonwealth of Pennsylvania, having jurisdiction to regulate rates and charges for the sale and distribution of gas pursuant to the Pennsylvania Public Utility Law, Act of May 28, 1937, P.L. 1053, 66 Purdon's Pennsylvania Statutes Annotated, 1101. This statute reposes in the Commission responsibility for the regulation of public utilities and for the preservation and protection of the public interest. The Pennsylvania Commission has an interest in any proceeding which affects the supply of natural gas and the rates charged to public utilities distributing gas within the Commonwealth of Pennsylvania.

Tennessee Gas Transmission Company is a major supplier of a number of such distributing companies and of their wholesale suppliers. The issues presented by the instant case, may have a substantial impact on the cost of gas to distributing companies and on the rates charged to ultimate consumers in Pennsylvania. Moreover, the outcome of such issues may affect action by the Federal Power Commission with respect to both pending and future proceedings

involving rates of other natural gas companies supplying gas to distributing companies in Pennsylvania and their wholesale suppliers.

Because of the broad impact of any decision rendered in this case on the rates to be charged to ultimate consumers in Pennsylvania, we urge the Court to reverse the decision below (Reported at 293 F. 2d 761).

STATEMENT OF THE CASE

The Petitioners request that this Court review a decision of the Fifth Circuit Court of Appeals which sets aside an order of the Federal Power Commission requiring an immediate reduction in rates and the refunding of that part of the increased rates collected subject to refund and found by the Commission's order to be excessive.

The history of the proceedings commencing with the order of the Federal Power Commission and the subsequent review by the Circuit Court is set forth in the Brief submitted by the Federal Power Commission.

Argument

ARGUMENT

The Pennsylvania Public Utility Commission is greatly concerned that the interim rate order procedure will be rendered ineffective if the decision of the lower court in the instant case is permitted to stand. The decision of the Court of Appeals would prevent the Commission from making use of an important procedural device to curtail increases, even after proven excessive, and to require appropriate refunds. The Commonwealth of Pennsylvania and the Pennsylvania Public Utility Commission are filing their amicus brief in this proceeding to urge this Court to protect the rights of their inhabitant consumers, as well as the rights of consumers everywhere that depend upon supplies of natural gas regulated under the Natural Gas Act, June 21, 1938, 52 Stat. 821; Title 15 U.S.C. 717-717w.

A. The Importance of and Necessity for the Interim Order Procedure in Rate Proceedings

A heavy burden has been placed on natural gas consumers by the increases in rates of natural gas companies made effective, subject to refund.¹ The chair-

¹ Under Section 4(e) of the Natural Gas Act, a natural gas company may file an increase in rates and, if the Commission should suspend it, the company may, by motion, make the increase effective after the five month suspension period elapses.

man of the Commission stated in August, 1962 that \$900,000,000 had been collected subject to refund in proceedings involving natural gas pipeline companies pending before the Commission. The Commission's press release, announcing the recent examiner's decision in the instant Tennessee case at Docket No. G-19983 noted that \$270,000,000 had been collected subject to refund under the rates made effective in Tennessee's three pending proceedings. It is estimated that the Tennessee increases aggregate \$64,000,000 a year over the last finally adjudicated Tennessee rates. Thus, the amount Tennessee collects subject to refund is growing at a rate of more than \$5,000,000 per month.

The Commission is charged with the duty under the Natural Gas Act of protecting consumers from excessive rates. This Court has said:

“... The (Natural Gas) Act was so framed as to afford *consumers* a complete, permanent and effective bond of protection from excessive rates and charges. . .” (Emphasis added.) (*Atlantic Refining Co. v. Public Service Commission of New York*, 360 U.S. 378, 388)

One form of consumer protection envisaged by Congress was that consumers should receive prompt relief from excessive increases in rates. Section 4(e) of the Natural Gas Act states in part:

“... At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural gas company, and the Commission shall give to the

hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible." (Emphasis added.)

The Commission's use of the interim rate order procedure is therefore of great import in effectuating the purposes which Congress sought to accomplish by its passage of the Act. It is incumbent upon the Commission to take whatever steps it can to alleviate "as speedily as possible" the burden imposed on consumers by rates made effective subject to refund. The interim order procedure permits early refunds and rate reductions to be made when a portion of an increased rate is found to be unjustified. The Commission developed and adopted this procedure because it knew full well that final disposition of rate increases must await lengthy administrative proceedings and possible judicial review. This Commission policy has been sanctioned by the Courts. In *Natural Gas Pipeline Company v. Federal Power Commission*, 120 F. 2d 625, affirmed, 315 U.S. 575, the Circuit Court urged the use of interim orders in rate proceedings, stating:

"... We must and do hold that upon a proper showing, and when the hearing has reached a stage where the Commission may determine that a reduction (or an increase) of rates should be made, it may (and should) make such order, even though the hearing be not completed."

In our opinion, the above language *directs* the Commission to use the interim order procedure wherever possible. This is in accord with the Act's mandate to decide rate questions "as speedily as possible".

The Commission is well aware that the question of a proper rate of return has an important bearing upon the overall allowable cost of service in a rate proceeding. The Commission is cognizant also, that disposition of this issue is a matter of discretion to be decided on the basis of evidence available to it from industry and public sources and testimony with respect thereto without reference to other issues concerning various aspects of the cost of service. In the instant case, the Commission correctly concluded, in view of the claimed allowance of 7% compared with historical allowances in the neighborhood of 6%, that an interim finding and order on the issue of rate of return would have a significant impact upon the allowable cost of service and the rates charged to Tennessee's customers.

The order of August 9, 1960, resulted in a reduction in the jurisdictional rates charged of \$11,000,000 annually. Since that order was issued, Tennessee's customers have received the benefit of refunds and reductions amounting to at least \$25,000,000. Thus the burden of increased rates has been substantially reduced through the interim order procedure and such benefit will continue as a direct result of such procedure until final determination is made of Tennessee's rates in these proceedings.

It is evident from the above, that without such a device, the natural gas companies would be enabled to continue to collect excessive rates and thus consumer interests would not be fully protected as was intended by the Act. It is noted that this Court has spoken of consumer rate protection as the "primary

aim of the Natural Gas Act" (*Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 610).

A public utility rate proceeding is almost invariably intricate and protracted and often involves various difficult issues. This necessitates extended hearings with a complex and voluminous record. Of necessity, a great deal of time is required for briefs, an examiner's decision, oral argument, the formulation of a final Commission decision and the court review which is not unusual in this type of proceeding. Unless relief is provided during this period of time, the rate payers would be burdened with the excessive rates until the final conclusion of the case.

The instant case is a good example of such a protracted proceeding. Tennessee filed for rate increases in 1957 (G-11980), 1958 (G-17166) and 1959 (G-19983). Under Section 4(e) of the Natural Gas Act, each of these increases was suspended for the statutory five month period. The increased rates subsequently went into effect and have been collected as filed, subject to refund, pending determination of their justness and reasonableness by the Commission. None have been finally decided.

Without burdening this Court with a mass of details as to the record in these proceedings, suffice it to say that after many days of hearings and conferences spanning a period of more than three years, the only action taken thus far, has been the issuance of an examiner's decision and Commission Opinion on cost allocation in the first docket;² and an interim

²The subject Opinion No. 352 was issued on February 6, 1962 almost eighteen months after the disputed interim order on rate of return was issued.

order on rate of return and an examiner's decision on cost of service issues in the third docket. Judicial review is pending on the allocation³ issue and exceptions have been filed on the cost of service issues. But this is by far not the end of the road. Still to be acted upon are exceptions to the examiner's recent decision. Hearings have yet to be held on rate design in Docket G-19983 and on cost of service, including rate of return, and rate design in Docket G-11980 and on all issues in Docket G-17166. We are aware that some of the procedural delay may be lessened by consolidation, but nevertheless, the issues must be dealt with.

In view of the above, it is evident that the Commission had more than sufficient reason to institute the interim order procedure without awaiting decision on any of the remaining issues.

Concurrently with the issuance of the examiner's recent decision in the third docket, he scheduled a settlement conference, currently in progress, embracing all three dockets in an attempt to bring an early conclusion to these proceedings and thus avoid the otherwise inevitable delay. As a matter of fact, a major effort has certainly been noticeable on the part of the Commission to settle pipeline rate cases without the need of the formal hearing procedure. This is another device by which the Commission is attempting to speed up the disposition of pending cases to produce *early rate reductions and refunds to consumers*. However, every case pending before the Federal Power Commission cannot be settled. Certain cases, as the instant one, because of controversy must of necessity go to hearing, and the Commission's

interim order is an instrument to provide similar benefits, i.e., *early rate reductions and refunds to consumers*. Yet the lower court seemed to ignore the above purpose of the Act when it stated that until the Commission fixes rates under Section 4(e), the consumer is protected by the refund of excess charges with seven percent interest. Obviously, a promise of future refunds does not protect consumers in the same manner as early refunds and rate reductions. We think that this was the Congressional intent when it directed speedy Commission decisions of rate questions. It certainly would be to no avail if the Commission merely apprised consumers of the fact that they were paying excessive rates and that refunds would be made some time in the indefinite future.

The refund provision is also inadequate because in addition to postponing relief from excessive rates, it deprives many consumers of the refunds to which they are entitled. Refunds by distributing companies are passed along to the consumers being served at the time the distributor receives refunds from the natural gas company. Because of shifts in population over a period of time, the consumer that paid the increase is often not there to receive this refund.

B. The Lower Court's Error

The Court below apparently recognized that the Commission had authority to issue interim orders. However, the majority was convinced that consumers would be adequately protected by Tennessee's refund obligation and that the Commission's interim order, in this instance, was unreasonable and an abuse of discretion because the Commission should have first decided the allocation issue; otherwise, the Court felt no basis existed for setting rates and Tennessee could suffer irreparable injury.

In our opinion, the Court below mistakenly subordinated the interests of consumers to the interests of Tennessee. We need not repeat here our view expressed above that Congress intended the Act primarily for the benefit of consumers. Yet, despite the Court's affirmance of the Commission's rate of return finding, it decided that consumers must wait until final decision of this case before refunds would be received.

The Court also erred in declaring that a decision on the allocation issue must precede any rate reduction and refunds. Aside from the Court's erroneous assumption that the issue was then ripe for decision, we submit that no such requirement existed. Tennessee received a full hearing on the rate of return question and failed to satisfy its burden of proof under the Act. We do not believe that the Act contemplated that the Commission must assume the bur-

den of proving that an increase unsupported by the company might be supportable by other possible evidence not yet adduced. In any event, there was reason to believe that other costs of service claimed by Tennessee were excessive. This is supported by the subsequent examiner's decision indicating that the excess was approximately \$25,000,000 annually. The order requiring the interim reduction and refunds was based on Tennessee's own claimed cost of service, other than rate of return, and its own allocation principles.

It so happens that the Commission's allocation decision issued subsequent to the interim order did not depart substantially from the method advocated by Tennessee. Notwithstanding the possibility that the Commission's final orders on cost allocation and cost of service could indicate that Tennessee is entitled to receive greater revenues in one or more rate zones than those collected under the interim order rates, we submit that Tennessee does not have a vested right to the revenues within a rate zone or overall revenues which would produce a $6\frac{1}{8}\%$ return. Although the Commission's order found an overall $6\frac{1}{8}\%$ return to be a just and reasonable allowance for Tennessee, which finding was affirmed by the lower Court, the Commission is not obligated to insure that Tennessee earns this return. It is within the Commission's discretion to order rate decreases to the lowest reasonable rates.

Section 5(a) of the Act states:

... the Commission may order a decrease where existing rates are unjust, unduly discrim-

inatory, preferential, otherwise unlawful, or are not the lowest reasonable rates."

By long standing usage in the field of rate regulation the "lowest reasonable rate" is one which is not confiscatory in the constitutional sense.³

In this connection, the Court of Appeals for the Eighth Circuit stated in *Panhandle Eastern Pipeline Co. v. Federal Power Commission* 143 F. 2d 488, 496:

"The last question for consideration is whether the return allowed by the Commission has been shown to be unjust, unreasonable or confiscatory.

"The opinion of the Supreme Court in the Hope Natural Gas Company cases indicates to us that, aside from questions relating to procedural due process and to jurisdiction, a reviewing court may interest itself only in the effect of the Commission's order. The court cannot concern itself with the Commission's choice of formulae or the propriety of the methods employed by it in reaching its conclusion, but only with the consequences of the order made. If the effect of the order is to deny to the utility a return sufficient reasonably to meet its necessities and to enable it to continue to render adequate public service, the order is arbitrary and confiscatory and may be set aside. It seems apparent that the Supreme Court is presently of the opinion that, within broad limits, the Federal Power Commission should be freed from judicial interference in regulating rates of nat-

³ See: *F.P.C. v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585; *Los Angeles Gas Corp. v. Railroad Commission*, 289 U.S. 287, 305.

ural gas companies. It is evidently no longer necessary for a reviewing court to consider many of the doubtful and debatable questions which ordinarily arise in every rate case.

"The order of the Commission must be affirmed unless the petitioners have made a convincing showing that it is unreasonable in its consequences because the return allowed is insufficient to enable them to meet their expenses of operation, to pay interest on their bonds and dividends on their stock, to maintain their credit and to attract capital or is clearly out of line with the returns on investments in enterprises involving comparable risks."

If we assume, *arguendo*, that Tennessee fails to earn a 6 $\frac{1}{8}$ % return under the rates established by the interim order, no injury may be claimed unless the overall return is reduced to the level of confiscation.

On this point, the Supreme Court in *F. P. C. vs. Natural Gas Pipeline Co.*, *supra*, stated:

"Assuming that there is a zone of reasonableness within which the Commission is free to fix a rate varying in amount and higher than a confiscatory rate, the Commission is also free under Sec. 5(a) to decrease any rate which is not the 'lowest reasonable rate'. It follows that the congressional standard prescribed by this statute coincides with that of the constitution, and that the courts are without authority under the statute to set aside as too low any 'reasonable rate' adopted by the Commission which is consistent with constitutional requirements."

The lower Court, in the present case, invalidated the Commission's interim order on the assumption that the retroactive effect of the final determination of the cost allocation issue will make it "highly unlikely, if not impossible, for a utility to earn a 'just and reasonable return'."

The Court not only fails to lay any foundation for this assumption, but has acted without the legal criteria declared necessary by this Court in the *Natural Gas Pipeline* case, *supra*:

We submit that rates not shown to be confiscatory cannot be set aside, and that the reasoning of the Court below on the interim order issue is contrary to both fact and legal precedent and can not be sustained.

The Commission's issuance of an interim order in this case was an attempt to satisfy the obligations placed upon it by the Natural Gas Act to protect consumer interests. We submit that the interim order was not unreasonable or an abuse of Commission discretion, but was in full accord with the requirements of the Act, Congressional intent and judicial precedent.

CONCLUSION

For the foregoing reasons, the decision of the Court of Appeals should be reversed.

Respectfully submitted,

HERBERT E. SQUIRES,

Assistant Counsel,

ALAN R. SQUIRES,

Assistant Counsel,

JOSEPH I. LEWIS,

Counsel,

Pennsylvania Public Utility
Commission

DAVID STAHL

Attorney General,

Commonwealth of
Pennsylvania

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute involved	2
Statement	3
The increased rate filing	3
Proceedings in the court below	7
Summary of argument	8
Argument	13
I. Under the Natural Gas Act, the Commission was empowered, upon determining that Tennessee's increased rates were predicated upon an excessive claim for rate of return, to issue an interim order disallowing the excess	15
A. Sections 4 and 16 give the Commission power to disallow, by interim order, that portion of an increased rate which the proponent has failed to justify	15
B. The presence of an unresolved allocation issue does not curtail the Commission's interim order powers	25
C. Provision for refund is not a satisfactory substitute for interim rate reduction	32
II. The Commission's interim reduction order was a reasonable and appropriate exercise of its statutory authority	36
A. The allocation issue was not ripe for Commission decision	38

Argument—Continued

B. There is no basis for the holding below that Tennessee would be prevented from earning the fair rate of return during the interim period.....	Page 39
III. The Columbia companies are not prejudiced by the interim rate reduction.....	41
A. The interim reduction left opportunity for hearing unimpaired on all issues other than rate of return.....	43
B. It is not necessary to continue excessively high rates in order to preserve power to correct discrimination.....	45
Conclusion.....	46
Appendix A.....	47
Appendix B.....	52
Appendix C.....	62

CITATIONS

Cases:

<i>Atlantic Refining Co. v. Public Service Commission of New York</i> , 360 U.S. 378.....	17
<i>Brimstone Railroad Co. v. United States</i> , 276 U.S. 104.....	31
<i>Brooklyn Savings Bank v. O'Neil</i> , 324 U.S. 697.....	34
<i>Central States Electric Co. v. City of Muscatine</i> , 324 U.S. 138, judgment amended, 325 U.S. 836.....	33
<i>Episcopal Theological Seminary v. Federal Power Commission</i> , 269 F. 2d 228, certiorari denied sub nom. <i>Pan American Petroleum Corp. v. Federal Power Commission</i> , 361 U.S. 895.....	22, 24

Cases—Continued

<i>Federal Power Commission v. Hope Natural Gas Co.</i> , 320 U.S. 591	Page 17
<i>Federal Power Commission v. Interstate Natural Gas Co.</i> , 336 U.S. 577	33
<i>Federal Power Commission v. Natural Gas Pipeline Co.</i> , 315 U.S. 575	10, 19, 22, 31, 33
<i>Hope Natural Gas Co. v. Federal Power Commission</i> , 196 F. 2d 803	35, 36
<i>Interstate Commerce Commission v. Inland Waterways Corp.</i> , 319 U.S. 671	19
<i>Interstate Power Co. v. Federal Power Commission</i> , 236 F. 2d 372, certiorari denied, 352 U.S. 967	29
<i>Manufacturers Light and Heat Co.</i> , 25 F.P.C. 595	42
<i>Manufacturers Light and Heat Co.</i> , 23 F.P.C. 446; petition to review dismissed sub nom. <i>Lynchburg Gas Co. v. Federal Power Commission</i> , 284 F. 2d 756	39
<i>Mississippi River Fuel Corp. v. Federal Power Commission</i> , 163 F. 2d 433	20
<i>Mississippi River Fuel Corp. v. Federal Power Commission</i> , 121 F. 2d 159	22, 24
<i>Montana-Dakota Utilities Co. v. Northwestern Public Service Co.</i> , 341 U.S. 246	17
<i>Natural Gas Pipeline Co. v. Federal Power Commission</i> , 141 F. 2d 27	33
<i>Natural Gas Pipeline Co. v. Federal Power Commission</i> , 134 F. 2d 263	33
<i>Natural Gas Pipeline Co. v. Federal Power Commission</i> , 131 F. 2d 137	33
<i>Natural Gas Pipeline Co. v. Federal Power Commission</i> , 129 F. 2d 515	33
<i>Natural Gas Pipeline Co. v. Federal Power Commission</i> , 128 F. 2d 481	33

Cases—Continued

	Page
<i>New England Divisions Case</i> , 261 U.S. 184.....	22, 31
<i>Northern Natural Gas Co.</i> , 11 F.P.C. 123.....	28-29
<i>Northern Natural Gas Co.</i> , 11 F.P.C. 278.....	28
<i>Northern Natural Gas Co.</i> , 11 F.P.C. 1324.....	29
<i>Northern Natural Gas Co.</i> , 13 F.P.C. 773.....	29
<i>Northern Natural Gas Co.</i> , 13 F.P.C. 1518.....	29
<i>Ohio Fuel Gas Co.</i> , 26 F.P.C. 213.....	42
<i>Panhandle Eastern Pipe Line Co. v. Federal Power Commission</i> , 236 F. 2d 606.....	22,
	24, 25, 30, 31, 38, 39
<i>Panhandle Eastern Pipe Line Co.</i> , 25 F.P.C. 787, affirmed in part and remanded in part C.A.D.C. No. 16583, decided June 30, 1962..	39
<i>Southern Natural Gas Co.</i> , 24 F.P.C. 26.....	39
<i>State Corporation Commission of Kansas v. Federal Power Commission</i> , 206 F. 2d 690, certiorari denied, 346 U.S. 922.....	22,
	24, 25, 28, 30, 31, 38
<i>Sunray Mid-Continent Oil Co. v. Federal Power Commission</i> , 364 U.S. 137.....	17
<i>Tennessee Gas Transmission Co.</i> , Docket No. G-19983, examiner's decision issued May 28, 1962 (unreported).....	14, 62
<i>Tennessee Gas Transmission Co.</i> , decided February 6, 1962; 42 P.U.R. 3d 145, pending on review sub nom. <i>Manufacturers Light and Heat Co. v. Federal Power Commission</i> , C.A.D.C. No. 17064.....	5, 38, 62
<i>Tennessee Gas Transmission Co. v. Federal Power Commission</i> , 283 F. 2d 729.....	7

Cases—Continued

<i>Tennessee Gas Transmission Co.</i> , Docket No. G-5259, order issued September 20, 1956 (unreported).....	Page 21
<i>United Fuel Gas Co.</i> , order issued March 20, 1962.....	42
<i>United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division</i> , 358 U.S. 103.....	15
<i>United Gas Pipe Line Co. v. Mobile Gas Service Corp.</i> , 350 U.S. 332.....	15

Statutes and Regulations:

Interstate Commerce Act, Section 15(7), 49 U.S.C. 15(7).....	12, 19, 35
Natural Gas Act, June 21, 1938, c. 556, 53 Stat. 821-833, as amended, 15 U.S.C. 717-717w.....	2, 15, 47
Section 4, 15 U.S.C. 717c.....	19
Section 4(a), 15 U.S.C. 717c(a).....	17, 47
Section 4(b), 15 U.S.C. 717c(b).....	17, 47
Section 4(c), 15 U.S.C. 717c(c).....	47
Section 4(d), 15 U.S.C. 717c(d).....	3, 47
Section 4(e), 15 U.S.C. 717c(e).....	9, 12, 15, 17, 18, 21, 27, 35, 43, 47
Section 5, 15 U.S.C. 717d.....	19
Section 5(a), 15 U.S.C. 717d(a).....	17, 19, 31, 47
Section 16, 15 U.S.C. 717o.....	9, 17, 19, 47
Section 19(b), 15 U.S.C. 717r(b).....	47
Transportation Act of 1920, 41 Stat. 456, Section 418(7), as amended, 49 U.S.C. 15(7).....	35
Federal Power Commission Regulations under the Natural Gas Act, Section 154.63, 18 C.F.R. 154.63.....	20

Statutes and Regulations—Continued

Federal Power Commission Rules of Practice
and Procedure, Section 1.30(c)3, 18 C.F.R.

1.30(c)3 ----- Page 5

Miscellaneous:

Hearings before House Committee on Inter-
state and Foreign Commerce on H.R. 4378,
66th Cong., 1st sess. ----- 35Hearings before Senate Committee on Inter-
state Commerce on the Extension of Tenure
of Government Control of Railroads, 65th
Cong., 3d sess. ----- 36Interstate Commerce Commission, *Twenty-
First Annual Report (1907)*: ----- 35MacVeagh, *The Transportation Act, 1920
(1923)*: ----- 361 Sharfman, *The Interstate Commerce Act
(1931)*: ----- 35, 36

In the Supreme Court of the United States

OCTOBER TERM, 1962

No. 48

FEDERAL POWER COMMISSION, PETITIONER

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY AND UNITED FUEL GAS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

OPINIONS BELOW

The orders of the Federal Power Commission (R. 524-540, 585-591) are reported at 24 F.P.C. 204 and 525. The opinions of the Court of Appeals for the Fifth Circuit (R. 635-646) are reported at 293 F. 2d 761.

JURISDICTION

The judgment of the Court of Appeals was entered on August 2, 1961 (R. 647). A petition for rehearing, timely filed, was denied on October 5, 1961 (R. 648). The petition for a writ of certiorari was filed

on December 8, 1961, and granted on January 22, 1962 (R. 660), 368 U.S. 974. The jurisdiction of this Court rests upon 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTION PRESENTED

Tennessee Gas Transmission Company, a natural gas pipeline company, filed increased rates predicated on a cost of service which included a claim to a 7 percent rate of return on net investment. After suspension by the Commission for the full five months permitted by law, the new rates went into effect subject to refund of any portion not ultimately justified by the pipeline company in the proceedings before the Commission. Several months later, the Commission, treating separately the issue of rate of return, found, after full hearing, that 7 percent was excessive and that $6\frac{1}{8}$ percent would be proper. It thereupon ordered a reduction, *pro tanto*, of the increased rates being collected subject to refund.

The question, which arises under Section 4 of the Natural Gas Act, is whether the Commission upon finding that one component of the company's justification for the increased rates is deficient may immediately order the rates reduced to that extent without awaiting the completion of all phases of the rate proceeding.

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821-833, as amended, 15 U.S.C. 717-717w, are set forth in the Appendix A, *infra*, pp. 47-51.

STATEMENT

The increased rate filing.—On October 5, 1959, Tennessee Gas Transmission Company, a natural gas company engaged in the pipeline transmission business, tendered increased rates for filing pursuant to Section 4(d) of the Natural Gas Act, *infra*, p. 48. These rates would result in an annual increase of \$26,590,138 in Tennessee's revenues based on sales for the year ended July 31, 1959 (R. 503).¹ The need for this increase was predicated upon a claimed cost of service which included a rate of return of 7 percent on net investment (R. 498-501).

By order of November 4, 1959, the Commission set a hearing to determine the lawfulness of these new rates and suspended their operation for the statutory maximum of five months (R. 502-505). The hearing started on February 2, 1960 (R. 524).² On

¹ This increase was in addition to previous increases (F.P.C. Docket Nos. G-11980 and G-17166) which are still pending before the Commission in rate proceedings. Those increases had become effective, subject to refund, on July 14, 1957, and May 15, 1959, respectively. The increased rates filed on October 5, 1959, were intended to produce about \$75,000,000 more in annual revenues than the rates last approved by the Commission. The lower figure mentioned in our petition for certiorari resulted from adding up the three increases computed on the basis of ~~rates~~ figures as of the time each set of increased rates was filed. The \$75,000,000 figure is derived by subtracting the revenues which would be produced by the last Commission-approved rates applied to test year sales figures (which are substantially in excess of the test year sales figures related to the earlier rates) from the revenues the interim rates would produce on the same sales figures.

² The Commission had originally ordered the hearing to commence on December 15, 1959 (R. 504), but by notice of November 16, 1959, granted Tennessee's request for a postponement.

April 5, 1960, at the close of the five-month suspension period and during the course of the hearing, the rates became effective, subject to an undertaking by Tennessee to make refund of any portion found by the Commission not justified, together with interest thereon (R. 505-509).

At the hearing, Tennessee presented all of its direct evidence. Its witnesses, however, were cross-examined only on the issue of rate of return. The staff of the Federal Power Commission and one intervenor, the West Virginia Public Service Commission, presented evidence only on the rate of return, and their witnesses were cross-examined. None of the other interveners sought to present evidence on rate of return. Tennessee then presented rebuttal testimony on rate of return; cross-examination on this testimony was concluded on May 25, 1960 (R. 524-525).

After all the evidence on rate of return had been presented, the Commission staff counsel moved that the proceeding be divided into two phases: (1) determination of rate of return; (2) determination of the various other factors entering into the company's cost of service and allocation thereof. He proposed further that, if it were found in the first phase that a proper rate of return was less than 7 percent, the Commission enter an interim order reducing Tennessee's rates *pro tanto* and directing corresponding refunds for the past.² Concurrently, staff counsel requested waiver of the examiner's intermediate decision on the issue of the rate of return (R. 525).

² This proposal contemplated acceptance of all of Tennessee's other claims for purposes of the interim order.

Tennessee opposed this interim order procedure, relying upon the fact that the proper method of allocating Tennessee's cost of service among its six zones was contested in this proceeding, and that in another proceeding relating to Tennessee's rates for an earlier period (F.P.C. Docket No. G-11980) the zone allocation issue had been tried and was awaiting decision by the hearing examiner (R. 591-606).⁵

On June 17, 1960, the Commission granted the motion to waive the intermediate decision on rate of return and provided for oral argument on that issue and on the question whether interim rate reductions and refunds should be ordered in the event that Tennessee's 7 percent figure was found excessive (R. 513-516). Thereafter, on July 19, 1960, Tennessee filed an untimely⁶ motion requesting the Commission to waive the intermediate decision procedure

⁵ Several interveners, including the other respondents here, also opposed this procedure (R. 607-625). The related proposal of waiver of the examiner's decision on rate of return was unopposed (R. 513).

⁶ Tennessee also pointed out that the hearing examiner in No. G-11980, who was also the examiner in this case, had ruled that determination of the zone allocation issue in that proceeding would govern the method of allocating costs among Tennessee's six zones in the instant case (R. 605). The Commission, when it decided the allocation issue in G-11980, expressed agreement with this procedure. *Tennessee Gas Transmission Co.*, decided February 6, 1962, 42 P.U.R. 3d 145, 146, 158.

⁷ The Commission's rules provide that motions requesting waiver of the examiner's intermediate decision shall be made no more than five days after conclusion of the hearings. 18 C.F.R. 1.30(c)(3). Hearings on the severed zone allocation issue in Tennessee's earlier case were concluded on December 17, 1959 (R. 522). The untimeliness of Tennessee's motion was referred to by the Commission in denying the motion (R. 522).

with respect to the zone allocation issue in the other proceeding (No. G-11980) and to decide that issue simultaneously with the rate of return issue in this proceeding (R. 519-521). This motion, which was opposed by a number of parties (including the Columbia companies,¹ R. 650-659) was denied on August 5, 1960 (R. 521-523).

On August 9, 1960, the Commission entered the order challenged below. It found that an overall rate of return of $6\frac{1}{8}$ percent was fair, just and reasonable for Tennessee (R. 526-535). Accordingly, it disallowed Tennessee's rates, computed by the company on the basis of the excessive (7 percent) rate of return. It specified, however, that the company might file interim reduced rates (R. 537-539) based upon the $6\frac{1}{8}$ percent rate of return and that such interim rates would become effective (subject to possible further refund at the conclusion of the entire rate proceeding) as of April 5, 1960, the date on which the disallowed rates had gone into effect. Refunds were to be made to the extent that the company had collected amounts in excess of said interim rates since April 5, 1960 (R. 539-540). The Commission pointed out that by permitting Tennessee to file substitute rates based on a proper rate of return, but otherwise based on the company's own claims, Tennessee and its customers would be placed in the same position as if Tennessee had originally filed increased rates predicated upon a proper rate of return (R. 535-536).

¹ Respondents, The Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company, who are members of the Columbia Gas System, are collectively referred to as the Columbia companies.

On September 27, 1960, the Commission denied applications for rehearing filed by Tennessee and the Columbia companies (R. 585-591). Both applications questioned the validity of the interim order procedure, and Tennessee also challenged the determination of the rate of return. The interim rates, which have resulted in an annual revenue reduction of about 10 $\frac{3}{4}$ million dollars, based on test year figures, have been collected since November 1, 1960.

Proceedings in the court below.—The court below unanimously affirmed the Commission's determination that a 6 $\frac{1}{8}$ percent rate of return was just and reasonable for Tennessee, but by a divided vote set aside the Commission order to the extent that it required Tennessee to make lower rates effective immediately and to refund the amounts collected in excess of the substitute rates.⁹

On the interim order issue, Judge Wisdom's opinion for the court (Chief Judge Tuttle dissenting, Circuit Judge Cameron concurring in the result only)¹⁰ concluded that, in the absence of a Commission decision on the zone cost-allocation issue, there was no basis for determining which of Tennessee's rates were unlawful; and that, although a natural gas

⁹ Stays of the reduction and refund order were denied by the Fifth Circuit, Judge Wisdom dissenting (R. 632-634; *Tennessee Gas Transmission Co. v. Federal Power Commission*, 283 F. 2d 729 (C.A. 5)). After its decision on the merits, the Fifth Circuit stayed its mandate until final disposition of the case by this Court (R. 648-649).

⁹ Tennessee has refunded \$7,416,663, plus interest, for the period from April 5, 1960, through October 31, 1960.

¹⁰ Chief Judge Tuttle wrote the part of the court's opinion affirming the Commission's rate of return decision.

company has the burden of justifying increased rates proposed by it, it "should not be held, at its peril, to the requirement of foretelling the decision of the Commission on the correctness" of such increased rates (R. 643). The opinion also states that, regardless of the Commission's authority, the allocation of costs among zones is "such an essential element in determining whether the filed rates are excessive" that issuance of the interim order in advance of decision on the allocation issue was an abuse of discretion (R. 643). Chief Judge Tuttle, dissenting, stated that he would have affirmed the Commission's order giving immediate effect to the conclusion that the rates based on an excessive rate of return were unreasonable. In his view, the applicant had the burden to establish each component upon which it predicated its rate increases, including the allocation of the cost of service to each of the rates filed. As a result of the interim order, Tennessee was in "no different position than if the Commission, after the section 4 hearing, decided that Tennessee was entitled to an overall return of 7 percent on its investment, just as asked for by Tennessee, but decided that the cost allocations between the several zones were discriminatory" (R. 646).

SUMMARY OF ARGUMENT

The Commission required Tennessee to reduce its increased rates without delay to the extent that they were predicated on an excessive claim (7 percent) for rate of return. For this purpose, the Commission assumed that Tennessee would be able to justify the increases insofar as they were controverted on

other grounds. In this way, the Commission, recognizing that other complex issues could not be resolved with equal expedition, sought to give substantial relief to the consumer promptly, while preserving the company's right to a full hearing and determination of all issues.

I. A. The Commission's rate powers under the Natural Gas Act are not limited to making final determinations of just and reasonable rates; it may also enter such orders "as it may find necessary or appropriate to carry out the provisions" of the Act. Section 16. Under the statutory scheme, the seller of natural gas initiates rates and rate changes. These rates, however, are subject to Commission review, and Section 4(e) expressly imposes upon the seller the burden of justifying increases. Here, Tennessee sought to support a set of increased rates on the basis of an overall cost of service, one component of which was a 7 percent return on net investment. As events proved, not more than $6\frac{1}{8}$ percent could be justified—a difference of \$11,000,000 per annum. At the time the interim reduction order was issued (four months after the increased rates had become effective), it was clear that disposition of the many other complex issues in the case could not be made until many months later and that consumers would continue to pay rates based on excessive claims if any reduction whatever had to await Commission determination of all issues in the rate proceeding.

In these circumstances, the Commission properly concluded that it had power to afford immediate relief to consumers, the primary beneficiaries of the

Natural Gas Act. Indeed, the courts have long approved the view that the Commission may require a company to file new or substitute rates, prior to the agency's final determination of just and reasonable rates, where the company's proof has failed to support its rates, either in whole or in part. See, e.g., *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 583-585.

The contrary view expressed in the opinion below gives no weight to the statutory provision requiring natural gas companies to provide a full justification of company-initiated rate increases. A company which files for increased rates must, under Commission regulations, make a full statement of all components of its cost of service—cost of purchased gas, labor, taxes, depreciation, return on investment, etc. A rate is not an indivisible entity but an aggregate of various components. If a company's proof fails to establish one of the ingredients upon which its claim to increased rates is predicated, those rates are, *pro tanto*, unsupported. This is the situation with respect to each of the Tennessee rates involved in this case.

B. The presence of an unresolved issue as to allocation of costs among zones does not curtail the Commission's authority to require an immediate reduction in rates that the company's showing has failed to justify. Tennessee's contention that because of that issue there is a possibility that it may not be able to recoup, for the refund period, the full revenues necessary to yield a $6\frac{1}{8}$ percent return

does not support delay in ordering Tennessee to submit rates which, based upon its own estimates and allocations, will provide that return. The eventuality (not shown to have any probability of occurrence) that Tennessee might not be able to secure all the revenues to which it is entitled is not a result of the interim rate procedure the Commission adopted; that could also occur, in the absence of an interim order, if it were found, at the conclusion of the entire case, that Tennessee, although justified in its claimed cost of service, was entitled to more than the filed rates in some zones but required to make full refunds in other zones. Moreover, Tennessee has no greater risk today than if it had originally filed rates based on a proper allowance for rate of return. Customers in no event have an obligation to provide a "cushion" so as to insure a natural gas company against the consequences of a discriminatory rate structure.

C. The court below assumed that the refund provision of the Act is a satisfactory substitute for an early reduction of excessive rates. But experience has shown that refunds do not afford full protection to the consumers who ultimately pay the excessive charges. Some will leave the area of service before the refund is made and passed on through the channels of distribution. In any event, for the ordinary consumer, even if he does not move, the impact of immediate increased costs is not neutralized by the prospect of repayment later. Moreover, since natural gas competes for markets with other fuels, the loss of business opportunities resulting from ex-

cessive rates (a loss which bears particularly upon pipeline customers for the gas and upon distribution companies) can never be restored.

The very fact that increased rates may be suspended for five months shows that Congress did not regard the refund provision as full protection for the consumer. This is also demonstrated by the history of the suspension and refund provisions in Section 15(7) of the Interstate Commerce Act, 49 U.S.C. 15(7), upon which Section 4(e) of the Gas Act is based.

II. The Commission's decision to enter an interim order was a reasonable exercise of its discretion. At the time that order was issued (August 9, 1960), the Commission was in no position to decide the allocation issue. Indeed, the preparation and issuance of opinions on that subject—first by the examiner and later by the Commission—required an additional eighteen months. The majority below erred, therefore, in its assumption that the allocation issue was "ripe for decision" when the interim procedure was adopted. Moreover, other substantial issues which bear on Tennessee's cost of service still remain unresolved.

III. There is also objection to the interim order from a single group of customers—the so-called Columbia companies. Columbia is of the view that Tennessee's rates in the zones in which Columbia purchases from Tennessee are discriminatorily high. It suggests that Tennessee should be permitted to collect the full increases for which it filed so that it will

have greater assurance of accumulating enough revenues to guarantee Columbia ■ all of the refunds to which Columbia may be held entitled at the conclusion of the rate proceeding. Columbia apparently believes that, if (a) it should establish wide discrimination as between zones and (b) the Commission should take the view that in all events Tennessee is entitled to a return of 6 $\frac{1}{8}$ percent for the past period involved, there might not be enough to pay it full refunds. For various practical reasons discussed *infra*, the hypothesis that there might not be enough revenues for the interim period to give Tennessee a fair return and to afford Columbia full refunds is a highly improbable one. In any case, however, the Commission has not undertaken to guarantee Tennessee a 6 $\frac{1}{8}$ percent return for the interim period. The determination that this figure represents a fair return does not constitute a holding that Tennessee is entitled to collect amounts sufficient to yield that return by means of a discriminatory system of rates.

Columbia also appears to argue that the Commission's interim order prejudices the issue of allocation of costs among zones. As the Commission's proceedings make plain, there is no basis whatever for this contention.

ARGUMENT

The Commission order under review required Tennessee to reduce its increased rates so as to eliminate that portion of those rates which reflected an excessive claim for return on investment. For purposes of its order, the Commission assumed the cor-

rectness of the other claims asserted by Tennessee in support of its increased rates. On the rate-of-return issue, it found, after a full hearing and oral argument, that a 7 percent rate was not justified and that $6\frac{1}{8}$ percent would be fair, just, and reasonable. Its determination on this point was unanimously affirmed by the court below and is not challenged in this Court.

Foreseeing that the complexity of the many other issues bearing on Tennessee's cost of service¹¹ and the problems involved in allocating that cost among Tennessee's zones would prevent a final determination of just and reasonable rates for a substantial period, the Commission ruled that Tennessee should not continue to collect its full increased rates predicated on a 7 percent rate of return until such a final determination could be made, but should, instead, file and collect substitute rates computed on the basis of a $6\frac{1}{8}$ percent rate of return (R. 537-540). It also

¹¹ The controverted issues on Tennessee's cost of service, aside from this rate of return issue, related principally to the income tax allowance, purchased gas cost adjustments, rate of depreciation, rate of return on production properties, and claims for off-pipeline system costs. Largely on the basis of these issues, the examiner has recently disallowed about \$25,000,000 of the cost of service claimed by Tennessee in addition to the \$11,000,000 involved here. *Tennessee Gas Transmission Co.*, F.P.C. Docket No. G-19983, decision issued May 28, 1962.

The complexity of these remaining cost-of-service issues is reflected by the length (165 pages) of the decision and the number of witnesses (31). Their testimony, covering about 3100 pages of transcript, took in excess of 18 days of hearing, over a period of more than one year, ending in April, 1961.

The testimony on rate of return, comprises about 1100 pages of transcript, requiring about 9 days of hearing spanning a period of about three months.

ordered, on the same basis, that the company refund the excessive amounts which had already been collected. In this fashion, the Commission sought to protect the ultimate consumer by reducing rates "as speedily as possible"¹² while also giving scope to the company's right to initiate new rates, to put them into effect (after the five-month suspension period) and to collect them until it has had its opportunity to justify them at a hearing.

1. UNDER THE NATURAL GAS ACT, THE COMMISSION WAS EMPOWERED, UPON DETERMINING THAT TENNESSEE'S INCREASED RATES WERE PREDICATED UPON AN EXCESSIVE CLAIM FOR RATE OF RETURN, TO ISSUE AN INTERIM ORDER DISALLOWING THE EXCESS *

A. Sections 4 and 16 give the Commission power to disallow, by interim order, that portion of an increased rate which the proponent has failed to justify.

1. Under the Natural Gas Act, as this Court has recognized, the seller of natural gas initiates its rates and rate changes. See *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332; *United Gas Pipe Line Co. v. Memphis Light, Gas and Water Division*, 358 U.S. 103. These rates are, however, subject to Commission review, and Section 4(e) of the Act expressly imposes upon the seller the burden of proving the justness and reasonableness of increased rates on such review:

* * * At any hearing involving a rate or charge sought to be increased, the burden of proof to

¹² Section 4(e), *infra*. App. A, pp. 48-49, provides that "the Commission shall give to the hearing and decision of such [increased rate] questions preference over other questions pending before it and decide the same as speedily as possible."

show that the increased rate or charge is just and reasonable shall be upon the natural-gas company * * *.

Tennessee here attempted to justify its increased rates (and thus meet its burden of proof) by showing an overall cost of service which included a return computed at a rate of 7 percent per annum on its claimed net investment. However, it failed to justify more than a rate of 6 1/8 percent, the difference amounting to about \$11 million a year. If the indicated \$11 million reduction in rates had to await decision of all of the other issues necessary to the fixing of just and reasonable rates, it could not have been prescribed by the interim order of August 9, 1960, which was issued some four months after the increased rates had gone into effect (subject to refund). Indeed, it could not have been ordered for many times four months thereafter; the complexity of the other cost-of-service issues and the intricate problems involved in allocating costs of service among zones made it unavoidable that the rate case, viewed in its totality, would be lengthy.

In these circumstances, the Commission properly concluded that consumer protection against excessive rates required something more than the issuance of an order prescribing just and reasonable rates at the distant end of the entire rate case. The agency had been given general powers to meet such needs; it had previously issued interim rate orders to meet similar demands; and such orders had uniformly been upheld by the courts.

The general power to meet such needs is granted by Section 16 of the Act, 52 Stat. 830, 15 U.S.C. §717o, which provides in part:

The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders * * * as it may find necessary or appropriate to carry out the provisions of this Act. * * *

Among the most important provisions of the Act "to be carried out" by the Commission,¹³ as the courts have repeatedly stated, are those designed to protect consumers against excessive rates. Sections 4(a), 4(b), 4(c), and 5(a), *infra*, pp. 47, 48-50. This Court has spoken of consumer rate protection as the "primary aim of the Natural Gas Act" (*Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 610; *Sunray Mid-Continent Oil Co. v. Federal Power Commission*, 364 U.S. 137, 147) and the "overriding intent of the Congress" (*Atlantic Refining Co. v. Public Service Commission of New York*, 360 U. S. 378, 389). At the same time, it has emphasized (*id.* at 388) the breadth of the powers given the Commission to provide that protection:

* * * The Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges. * * *

Thus, the provision of Section 4(e) relating to rate increases pointedly places the burden of proof on

¹³ As this Court has made clear, the rate standards of the Act are to be administered by the Commission, not the courts, in the first instance. *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-252.

the company and gives priority to Commission disposition of these matters.

In this case, the time which the Commission foresaw would be required to reach a final decision on all of the other issues would have meant a prolonged delay in affording protection to the consumer against Tennessee's exaction of a clearly illegal rate of return. The dollar amount of the reduction which turned on the rate-of-return issue was plainly of sufficient moment to justify the procedures involved in giving immediate effect to the Commission's determination. The protection which would have been afforded by the only alternative (refund) would have been much less satisfactory, for the reasons discussed *infra*, pp. 32-34. In such circumstances, to remain inactive would not "carry out" the Commission's statutory role; to allow Tennessee to continue to collect a 7 percent rate of return after its illegality was demonstrated would fail to provide "protection of consumers against excessive rates"; to try to decide *all* of the issues before making *any* reduction would miss "the primary aim of the Act." Since an immediate *pro tanto* reduction was clearly appropriate, the Commission had power to order it under Section 16.

2. The court of appeals has read the Act narrowly—as one authorizing the Commission only to make final determinations prescribing just and reasonable rates. Section 4(e), to be sure, authorizes the Commission to "make such orders with reference [to the changed rate] as would be proper in a pro-

ceeding initiated after it had become effective.” *Infra*, App. A, p. 49. This provision permits the Commission to do what it could do under Section 5(a) of the Act, *infra*, App. A, p. 49, which states that if the Commission finds a rate to be “unjust, unreasonable, unduly discriminatory, or preferential; the Commission shall determine the just and reasonable rate * * * to be thereafter observed and in force, and shall fix the same by order * * *.” But in a Section 5(a) proceeding, the Commission may take intermediate steps before resolving all questions which must be decided in order to fix just and reasonable rates; it can promptly effectuate a *pro tanto* reduction based on the company’s failure of proof in particular respects. *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 583-585. In any event, although the procedure outlined in Section 5 may be followed in a proceeding under Section 4, there is no obligation to pursue it.¹⁴ Section 16, as pointed out above, explicitly grants the Commission authority to enter such other orders as may be necessary or appropriate to carry out the basic statutory purposes.

¹⁴ Compare *Interstate Commerce Commission v. Inland Waterways Corp.*, 319 U.S. 671, 688-690. There, this Court held that under Section 15(7) of the Interstate Commerce Act—the suspension and hearing provisions upon which Section 4(e) of the Natural Gas Act is based—the Interstate Commerce Commission was not obliged to determine proportional rates although the section provided, as here, that the Commission *might* make such orders in suspension proceedings as would be proper in a proceeding initiated after the rate had become effective.

In holding that, in the absence of a Commission decision on cost allocations, there was "no basis for determining which of the filed rates in specific zones were unlawful" (R. 642), the court below misconceived the test of validity applicable to an interim order. For the test is not whether there can be a resolution of all questions which relate to the lawfulness of the rate but whether the sufficiency of the attempted justification of a component part of the increased rate can be decided separately. The decision below fails to recognize that pipeline rates, whether company-made or Commission-made, need not be regarded as indivisible entities, but may realistically be treated as aggregates of severable components. Their nature was aptly described in *Mississippi River Fuel Corp. v. Federal Power Commission*, 163 F.2d 433 at 450 (C.A.D.C.):

* * * Our law has never provided that either a company, a commission, or a court can fix a price for a utility commodity or service by an abstract observation or by a comparative evaluation of current prices for other commodities or services, or by any such process. The character of the rate has always been determined, in our law, by its relationship to the sum of a number of components.

Indeed, Tennessee, as a part of the filing of its increased rates here, was required by Section 154.63 of the Commission's regulations, 18 C.F.R. 154.63, to include a full and detailed account of the manner in which it had derived the increased rates which it proposed to charge. This included disclosure of all components of its claimed cost of service, such as

cost of purchased gas, labor, taxes, depreciation, return on investment and allocation of costs between jurisdictional and nonjurisdictional business and among zones and classes of service. Return on investment, in turn, is derived by determining a fair rate of return and applying that rate to net prudent investment, after making appropriate deductions for accrued depreciation. It follows that if, upon hearing the company's justification of one component fails, the increased rates are, to that extent, unsupported and need not be allowed by the Commission.¹⁵ To that extent, the burden of proof which Section 4(e) imposes on the company—a burden, in this case, of justifying the rates in each zone—has not been met.¹⁶

3. In prior instances where it has appeared that the proof failed to support, in whole or in part, the rates under investigation, the courts have approved the Commission's use of measures similar to the interim order

¹⁵ The court below (R. 642), as well as the petitioners in that court (respondents here), sought to rely upon a Commission order in an earlier Tennessee rate proceeding, in which the Commission denied Tennessee's request to fix rates prior to a determination of the zone allocation issue. See *Tennessee Gas Transmission Co.*, Docket No. G-5259, order issued September 20, 1956 (unreported), *infra*, App. B, pp. 52-61. But for the Commission to have granted Tennessee's request there would have been to purport finally to fix just and reasonable rates without hearing on, and justification of, the allocation of cost of service, *i.e.*, to prescribe partially unjustified increased rates, and not, as here, partially to disallow increased rates for failure to justify that part.

¹⁶ As earlier noted, the substitution of $6\frac{1}{8}$ percent for the 7 percent rate-of-return figure utilized in Tennessee's computations produces the substitute interim rates which are now in effect.

at issue in the present case. *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 583-585; *Panhandle Eastern Pipeline Co. v. Federal Power Commission*, 236 F. 2d 606 (C.A. 3); *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F. 2d 690, 715-716 (C.A. 8), certiorari denied, 346 U.S. 922; cf. *New England Divisions Case*, 261 U.S. 184, 199-201; see also *Mississippi River Fuel Corp. v. Federal Power Commission*, 121 F. 2d 159 (C.A. 8); *Episcopal Theological Seminary v. Federal Power Commission*, 269 F. 2d 228 (C.A.D.C.), certiorari denied *sub nom. Pan American Petroleum Corp. v. Federal Power Commission*, 361 U.S. 895.

In *Federal Power Commission v. Natural Gas Pipeline Co.*, *supra*, this Court affirmed an interim reduction of rates pursuant to a Section 5(a) investigation. It held (315 U.S. at 584) that a company which had presented its entire direct testimony in support of its rates could not complain that it had not yet been able to examine Commission witnesses on aspects of the case which, for purposes of the interim order, the Commission had decided on the basis of the company's presentation.

In *Panhandle Eastern Pipe Line Co. v. Federal Power Commission*, *supra*, like this one a case arising under Section 4 of the Natural Gas Act, the Commission eliminated a portion (approximately \$5,000,000 annually) of Panhandle's increased rates after the company had presented its case in chief. In taking this action, the Commission relied on its disallowance of the same components in the preceding *Panhandle* rate case and pointed out that no new or supervening

occurrences had been shown to warrant reconsideration of the Commission's recent decision. The Third Circuit, rejecting Panhandle's contention that no reduction could be ordered until all phases of the case had been resolved, held that a company which fails to make out a prima facie case in support of its cost of service is not entitled to continue collection of the unproved portion of its rates. The court pointedly observed (236 F. 2d at 608):

* * * Panhandle must have based its claim for a higher rate of return upon justification existing at the time of filing. It is difficult to see how else a change could have been proposed in good faith. True, in recognition of the time involved in these often long drawn out rate proceedings, the commission quite properly permits the basic showing of the justification which existed at the time of filing to be supplemented by evidence of occurrences since filing. But this is far from saying that a party who tries and fails to make a prima facie showing to support severable elements of his claim is entitled to a postponement of adjudication thereon in anticipation of possible new justification which some future event may supply before the overall case can be completed.

Here the record shows that Panhandle was given full opportunity to offer all of its evidence in support of the items which the commission disallowed in the order now on appeal. Thereafter, the commission was under no obligation to postpone its ruling on those matters. Indeed, to have done so would have permitted Panhandle to put into effect, albeit under bond and subject to possible future refund, increased

rates, parts of which it had attempted and, in the commission's view, failed to justify.

In the *State Corporation Commission* case, *supra*, the Eighth Circuit affirmed the Commission's interim reduction of increased rates filed by Northern Natural Gas Company to reflect the disallowance of \$7,601,853 of the company's claimed cost of service. As in the *Panhandle* case, the portion disallowed consisted of components which the Commission had rejected in Northern's preceding rate case and as to which the Commission found, after presentation of Northern's affirmative case, that no intervening changes had been shown warranting different treatment. In approving the Commission action, the court stated (206 F. 2d at 716):

* * * It is evident from the record therefore, that if the Commission had allowed the \$7,601,853 items to remain pending in Northern's third rate increase schedule the [preceding] Orders disposing of the same items would have been practically nullified. Northern's proposal was to continue indefinitely to charge its customers on the basis of its disallowed increase of \$7,601,853, regardless of adverse decision upon it by the Commission. Its position for aught that appears would justify its continuing the same course, notwithstanding judicial affirmance of the Commission. We do not think the statute can be construed to permit such a course of procedure by Northern.

Here, rather than reinstating the rates which had been in effect prior to the disallowed increased rates (as was done in the *Mississippi River Fuel Corp.* and *Episcopal Theological Seminary* cases, cited *supra*,

p. 22), the Commission permitted Tennessee to file substitute increased rates predicated on a total cost of service which included a $6\frac{1}{8}$ percent rate of return, but otherwise based on Tennessee's original presentation (the course followed in the *State Corporation Commission* and *Panhandle Eastern* cases, *supra*, p. 22).

B. The presence of an unresolved allocation issue does not curtail the Commission's interim order powers

Respondents argue that cases upholding interim rate orders are inapplicable because there is an unresolved issue in this case as to the allocation of the company's total costs. We disagree with this conclusion.

The contention is that, because of the allocation issue, there is a possibility that Tennessee may not be able to recoup, for the refund period, its full cost of service as found by the Commission. That possibility¹⁷ stems from the fact that conceivably the Commission might so decide the zone allocation issue and the remaining cost of service issues as to allow rates for customers in some of Tennessee's six rate zones higher than the interim rates now being charged, even though the over-all rates prescribed would pro-

¹⁷ Since the Commission proceedings had at that time been concluded only with respect to the rate-of-return issue, these substitute rates were to go into effect, subject to refund, as of the date the disallowed rates had become effective, *i.e.*, April 5, 1960.

¹⁸ However, as we indicate below, pp. 40-41, Judge Wisdom, speaking for the court below, did not have a sound basis for his view that the retroactive application of the cost allocation decision would make "it highly unlikely, if not impossible, for a utility to earn a 'just and reasonable return.'"

duce less total revenues than the interim rates. If that were to happen and refunds were to be ordered on the basis of such rates, Tennessee might not recoup a return of $6\frac{1}{8}$ percent because it would not be able to collect retroactively the higher rates found proper for some zones although it would be required to make full refunds in the other zones.

As the Commission pointed out (*supra*, p. 6), however, Tennessee's risk is no greater than it would have been if its increases had originally been predicated on a proper rate of return, *i.e.*, the $6\frac{1}{8}$ percent rate determined by the Commission and unanimously approved by the court of appeals. The possibility that Tennessee's method of allocation may have caused it to propose lower rates in some zones than the Commission might subsequently allow in no way vitiates the validity of the interim rate reduction order. For such a risk exists in every rate case, even where all issues are decided simultaneously.¹⁹ As Chief Judge Tuttle cogently observed in his dissent (R. 646):

* * * Tennessee stands in no different position than if the Commission, after the section 4 hearing, decided that Tennessee was entitled to an overall return of 7 percent on its investment, just as asked for by Tennessee, but decided that the cost allocations between the several zones were discriminatory, as here claimed by Columbia. * * * In such a situation Tennessee would not realize the full per-

¹⁹ Indeed, Judge Wisdom recognized (R. 642-643) that such a risk would exist even if the company's claimed cost-of-service were allowed in full.

mitted rate of return because it would have failed to substantiate the correctness of the cost allocation.

Thus the risk that Tennessee runs, and on which the opposition to the interim order rests, is not attributable to the interim order but inheres in the nature of the allocation issue. To be sure, if a company has been using impermissible methods of allocating its costs and has thereby discriminated among customers located in different areas, the Commission might be obliged to fix higher rates for particular zones (although a more likely outcome might be the fixing of *lower* rates for other zones) than those which the company has been collecting during the pendency of the rate proceeding. But that is a company risk—not one against which its customers should be required to furnish insurance by paying excessive charges.

The crucial consideration, as urged above, *supra*, pp. 15-21, is that under Section 4(c) the natural gas company has the burden of justifying the increases for which it has filed. The interim order is merely a prompt method of assessing the result of a failure to bear that burden. The opinion of Judge Wisdom (R. 643) erroneously assumes that the Commission, in finding that it would be proper for a company to earn a particular rate of return, guarantees that such a return will be earned. To the contrary, the Commission's conclusion as to the propriety of a particular rate of return means only that such a return was deemed proper on the basis of a test year and that rates designed to produce such a return in the future

are permissible.²⁰ As the Commission notes (R. 536), the company certainly cannot complain if the Commission orders that it discontinue collecting revenues which it has not justified on the basis of its own theory and evidentiary presentation.

Respondents also err in their attempt to distinguish the earlier interim order cases on the ground that no issue of zone allocation remained open there. In fact, the interim orders in the *State Corporation Commission* and *Panhandle* cases, *supra*, p. 22, did not preclude determination of final rates by the Commission on different allocation bases than those used by the company in fixing its interim rates.

In the *State Corporation Commission* case, the interim order affirmed by the court had been issued by the Commission in F.P.C. Docket No. G-1881. See *Northern Natural Gas Co.*, 11 F.P.C. 278 (Commission Opinion No. 233). In that proceeding, the Commission disallowed substantial portions of the company's increased rates because they were based on contentions that had been rejected by the Commission 75 days earlier in dealing with Northern's rates for earlier periods. See *Northern Natural Gas*

²⁰ Rates designed to recoup a particular estimated cost of service may, in fact, yield revenues which are either higher or lower than the actually experienced cost of service depending on such factors as the realization of estimated sales volumes, and changes in labor and material costs to levels other than those estimated. If the revenues realized are less than those anticipated, the company has no right to demand retroactive compensation for that reason, while the natural gas consumer can obtain no reparations if the actual revenues exceed either estimated costs or revenues.

Co., 11 F.P.C. 123 and 375 (F.P.C. Docket Nos. G-1382 and G-1533, Opinions No. 228 and 228-A). The Eighth Circuit, in the same opinion in which it affirmed the interim order, approved this prior Commission decision in most respects, but nonetheless set it aside for inadequate findings on rate of return. While the Commission, in issuing its opinion in the earlier proceedings, had found that the evidence presented by various parties to support zone rates for Northern's system was insufficient, nevertheless it specifically indicated, as noted by the court (206 F. 2d at 712), that the zone question could appropriately be reconsidered in the then pending Docket No. G-1881 proceeding in which the interim order was later issued. 11 F.P.C. 123 at 140.

The question of zone allocations thus was a very live issue in the Commission proceeding in which that interim order was issued. Moreover, nothing in the interim order (11 F.P.C. 278 and 1324) even suggests that zone rates sought by various interveners might not be ordered in the second phase of the proceeding and be applicable in the refund period.²¹ Although

²¹ Following the action of the Eighth Circuit setting aside the Commission's Opinion 228 on the ground that the findings were insufficient to support the rate of return allowance (206 F. 2d at 723), the rate proceedings involved in the interim order, as well as the two earlier dockets, were settled by the parties, with Commission approval. *Northern Natural Gas Co.*, 13 F.P.C. 1518. Accordingly, the zone question was not resolved until subsequent rate proceedings, when Northern was required to have zone rates. See *Interstate Power Co. v. Federal Power Commission*, 236 F. 2d 372 (C.A. 8), certiorari denied, 352 U.S. 967. In that later proceeding the parties agreed to make new zones effective prospectively only. See *Northern Natural Gas Co.*, 13 F.P.C. 773, 774.

respondents' precise contentions were not made in attacking the interim order, it is apparent that the *State Corporation Commission* case involved the same risks to Northern that Tennessee complains of here.

Similarly, the Commission's interim rate reduction order in the *Panhandle case* (236 F. 2d 606, C.A. 3), *supra*, did not preclude adjustments, in the second phase of the proceeding, which could result in rates higher than the interim rates. For while the Commission there concluded that Panhandle had not made out a case in support of certain changes in allocation and rate design methods, the interim order did not foreclose other parties to the proceeding from showing that the allocation and rate design that underlay Panhandle's interim rates should be modified. Quite aside from zone allocation issues, moreover, the court's opinion in the *Panhandle case* indicates that the company's contentions in that case were similar to Tennessee's here. As here, the company was urging that it should be allowed to continue collecting rates that it could not justify because rates at the same level might eventually be justified on the basis of evidence presented by other parties or because of changed circumstances.

Indeed, it is invariably true that the "other issues" (there are, of course, many issues in a typical rate case) which remain whenever the interim order procedure is invoked might conceivably result in an offset even if there were no allocation issue, *i.e.*, the rate proponent might be able to prove that, although some elements in the cost of service accepted by the Commission for the purposes of the interim order were

overstated, others were underestimated, with even large dollar effect. This could occur even in a Section 5(a) proceeding such as was involved in the *Natural Gas Pipeline* case; *supra*. In that event, the company would collect less from all of its customers during the period between the interim order and the later order than might ultimately be found just and reasonable with respect to that period, with no possibility of collecting such higher rates retrospectively. Thus the presence of an unresolved allocation issue does not distinguish this case from the earlier interim order cases.

Moreover, it is clear that questions of cost allocation loom as potential issues in virtually every major pipeline rate case. If interim rate reduction orders were to be limited to cases in which allocation issues could not be raised by any party in the later phases of a proceeding, the procedure could never be utilized, regardless of how excessive a pipeline's cost of service claims might be, and the holdings of the *State Corporation Commission* and *Panhandle* cases could not be justified.

As both the earlier cases and the situation here show, the interim order procedure is a useful and important tool in the Commission's disposition of proceedings involving increased rates. Public utility

²² It also appears that the Interstate Commerce Commission's failure to fix specific divisions in the *New England Divisions Case*, 261 U.S. 184, would have prevented carriers, if the resulting divisions were upset by the Commission, from collecting their fair share prior to the date of a new commission order. See *Brimstone Railroad Co. v. United States*, 276 U.S. 104.

rate proceedings are almost invariably complex and protracted, involving many parties and numerous difficult issues. Some of these issues, if severed, may be heard and determined more quickly than others. For it may be possible to decide some issues on the basis of prior decisions involving the same company or comparable questions of law, or on the basis of a relatively brief presentation of expert testimony. In contrast, other issues characteristically require extensive preliminary study and investigation by lawyers, engineers and accountants as well as lengthy and elaborate presentation at the hearing. As a result, the final resolution of all issues in a rate proceeding may take many additional months even though every effort is made by the Commission to expedite the case. To require all issues to be decided simultaneously would mean that rates based on clearly excessive claims must remain intact during the interim. It would thus impair Congress' purpose in providing that increased rate questions shall be decided "as speedily as possible" and its object of relieving the ultimate consumer of the burden of excessive pipeline charges.

C. Provision for refund is not a satisfactory substitute for interim rate reduction

The decision below seems to rest in large measure on the erroneous view that consumers are adequately protected, although they continue to pay excessive rates, by the pipeline's ultimate obligation to refund excess charges with interest. But refund provisions, like stays *pendente lite*, are by no means a satisfac-

tory substitute for the interim reduction of excessive rates. The courts' experience with the disposition of funds impounded as a result of judicial stays of Commission rate-reduction orders provides ample proof of this.²³

The consumer who bears the burden of excessive rates is not afforded full protection. For in today's mobile society, the consumers of natural gas who pay excessive rates in a given area today are scattered as the months go by. And it is our understanding that it is seldom feasible for distribution companies to refund excess amounts collected to the particular consumers who paid them. Rather, the refunds, either by a direct payment or credit on current bills spread over a period of months, are given to those consumers who are purchasing gas at the time of the refunds and on the basis of their current purchases. Moreover, for the ordinary consumer, even if he does not move, an immediate increase in his cost of living cannot be presumed to be offset by the prospect of receiving repayments some-

²³ The complexities and inadequacies of refunds seldom are reflected in the reported decisions but the reports relating to the refunds which followed the affirmance of the Commission's order in *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, are suggestive. A series of orders (all in *Natural Gas Pipeline Co. v. Federal Power Commission*, C.A. 7, No. 7454) are reported at 128 F. 2d 481, 129 F. 2d 515, 131 F. 2d 137, 134 F. 2d 263, 141 F. 2d 27. This Court dealt with the disposition of those impounded funds in *Central States Electric Co. v. City of Muscatine*, 324 U.S. 138 and 325 U.S. 836. See also the diverse opinions with respect to refunds in *Federal Power Commission v. Interstate Natural Gas Co.*, 336 U.S. 577.

time in the future. *Cf. Brooklyn Savings Bank v. O'Neil*, 324 U.S. 697, 707-708.

There is another important consideration. Natural gas is in competition with other fuels for industrial, commercial, and domestic consumers. As a consequence, the maintenance of excessive rates, albeit subject to refund, may prevent local distributing companies from attracting new customers and, by the same token, prevent such potential customers from using natural gas. Since the decision as to which fuel is to be utilized involves substantial investment—for example, in space-heating equipment or in air conditioning units—the loss of customers to other fuels because of an excessive price would tend to be permanent and could not be remedied by later refunds. Refunds to commercial and industrial consumers, of course, can never restore to them the business opportunities and competitive advantages lower fuel costs might have given them at the time they had to pay the excesses.

The structure and language of the Act show that Congress was well aware of the imperfect nature of the refund protection for customers. This is demonstrated in the first instance by the fact that the rate proponent can put a new rate into effect only after thirty days' notice and then only if the Commission does not suspend such a rate's effectiveness for a further period of five months. If the refund provisions had been considered a full equivalent of early reduction of excessive rates, there would have been no occasion to provide for a suspension or notice period.

The origin of the refund provisions in section 15(7) of the Interstate Commerce Act, 49 U.S.C. 15(7), upon which Section 4(c) of the Natural Gas Act was modeled (see *Hop v. Natural Gas Co. v. Federal Power Commission*, 196 F. 2d 803 (C.A. 4), shows, indeed, that the suspension provision was the primary *consumer* protection provided by that section, while the refund provision was added principally to protect the *carrier*. The suspension provision of the Interstate Commerce Act (49 U.S.C. 15(7))²⁴ was added in 1910 because reparations were deemed an inadequate remedy for the shipper.²⁵ See I Sharfman, *The Interstate Commerce Commission* (1931), pp. 58-60, 201-202; Interstate Commerce Commission, *Twenty-first Annual Report* (1907), pp. 9-10. The Interstate Commerce Act was thereafter amended to reduce the maximum suspension period to five months and to permit increased rates to become effective subject to refund provisions, before the end of the rate investigation. Section 418(7) of the Transportation Act of 1920, 41 Stat. 456, 486, as amended, 49 U.S.C. 15(7). These modifications were adopted because it was recognized that, particularly in a period of rising costs, an unduly long suspension period gave inadequate protection to the carrier, which would be unable to collect higher rates retroactively even though it were later found that the filing had been justified. See Hearings before House Committee on Interstate and Foreign Commerce on H.R. 4378, 66th Cong., 1st

²⁴ The 1910 amendment permitted suspension for a total of ten months.

sess., pp. 30-32; MacVeagh; *The Transportation Act, 1920* (1923), pp. 371-380; 1 Sharfman, *op. cit.* at pp. 201-202; *Hope Natural Gas Co. v. Federal Power Commission*, 196 F. 2d 803 (C.A. 4). During these hearings, it was recognized, however, that the refund provision would afford little more protection to the shipper and his customers than the reparations remedy previously found inadequate. This history shows a legislative attempt to accommodate competing interests but certainly evinces no belief that either refunds or reparations represent a fully adequate substitute for measures which prevent excessive rates from being collected in the first instance. See Hearings on H.R. 4378, *supra*, at pp. 30-32, 1527; Hearings before Senate Committee on Interstate Commerce on the Extension of Tenure of Government Control of Railroads, 65th Cong., 3d sess., Vol. 1 at 512.

II. THE COMMISSION'S INTERIM REDUCTION ORDER WAS A REASONABLE AND APPROPRIATE EXERCISE OF ITS STATUTORY AUTHORITY

The suggestion in the opinion below (R. 643) that, regardless of the Commission's authority to issue an interim order, it was an abuse of discretion to issue the order before deciding a pending allocation issue "ripe for decision" is also in error.

A. The allocation issue was not ripe for Commission decision

Judge Wisdom's opinion assumes that at the time the Commission required the interim reduction, it was in a position to decide the zone allocation issue. In fact it was not. To be sure, when the interim order

was issued on August 9, 1960, the examiner had heard all of the evidence on the matter of zone allocation in the related Tennessee rate case (covering a prior period, F.P.C. Docket No. G-11980). Moreover, he had stated (see, *supra*, p. 5, n. 5) that his decision on the zone allocation issue in that earlier rate case would also be applicable in this case. Nonetheless, the matter was not ready for Commission decision. The zone allocation issue in No. G-11980 had produced 4,500 pages of transcript (presented on more than 30 hearing days) and some 60 exhibits. The interests of more than ninety interveners were involved. Final briefs had been filed with the examiner on April 11, 1960. When Tennessee on July 19, 1960, moved to omit the examiner's intermediate decision, the Commission denied the motion explaining, *inter alia*,²⁵ that (R. 522-523):

* * * the nature and considerable size of the record, indicates that it would be more practicable in the interests of an early decision and in the interest of the effective administration of the Natural Gas Act, that the Presiding Examiner, who has available knowledge of that record, should proceed with consideration of the evidence and render decision thereon.

As events developed, the examiner was not able to render his decision, comprising 131 pages of text, until February 13, 1961 (more than six months after the interim order in the instant proceeding). Not until February 6, 1962, a year later, and after two

²⁵ It also noted the opposition (R. 650-659) of several of the parties to this request and the untimeliness of the motion.

arguments before it, including reargument in September 1961, was the Commission able to render its decision.²⁰ See *Tennessee Gas Transmission Co.*, decided February 6, 1962, 42 P.U.R. 3d 145, 146, 158. These facts in themselves show that the Commission had good reason, in the interest of expedition, to put its rate of return determination promptly into effect, without either awaiting the examiner's zone allocation decision or attempting to decide that issue simultaneously with the rate of return question.

Judge Wisdom's assumption that the allocation issue was ripe for decision by the Commission at the time the rate of return question was resolved overlooks the fact that not all issues as to which the taking of evidence has been completed are equally susceptible of prompt disposition. Some issues in public utility rate proceedings may be determined shortly after submission of the evidence. Thus, as in the *State Corporation Commission* and *Panhandle* cases, it may be possible to decide issues with dispatch on the basis of a prior decision involving the same company. Other issues may be decided quickly because of the familiarity achieved by the Commission in dealing with comparable questions of law or fact in other cases. Of course, only the deciding tribunal is in a position to determine what issues in a case it

²⁰ Applications for rehearing were denied on April 5, 1962. On June 4, 1962, a petition for review was filed by the Columbia companies challenging this decision. *Manufacturers Light and Heat Co., et al. v. Federal Power Commission*, C.A.D.C. No. 17064.

can decide more expeditiously than others. Here, it may be noted, however, that a decision on rate of return involves many comparisons common to the entire industry and that the rate of return for two other natural gas pipelines had been determined by the Commission earlier in 1960, not long before the interim order deciding the rate of return issue here. See *Manufacturers Light and Heat Co.*, 23 F.P.C. 446, petition for review dismissed *sub nom. Lynchburg Gas Co. v. Federal Power Commission*, 284 F. 2d 756 (C.A. 3); *Southern Natural Gas Co.*, 24 F.P.C. 26.

Other issues, such as the zone allocation issue here involved, may defy rapid disposition despite the best efforts of all concerned. But since the company-made rates necessarily are designed after determining a cost of service made up of severable components, there is no reason for permitting the full amount of such rates to be collected simply because one or more of the many issues in the case cannot be quickly resolved.²⁷

B. There is no basis for the holding below that Tennessee would be prevented from earning the fair rate of return during the interim period

For the reasons given above, pp. 25-32, we do not think that the possibility or even the probability that Tennessee might not be able to recoup the entire

²⁷ In the *Panhandle* case, *supra*, the interim order, disallowing about five million dollars of the claimed cost of service, preceded by 4½ years the Commission decision on the remaining issues in that case, *Panhandle Eastern Pipe Line Co.*, 25 F.P.C. 787, affirmed in part and remanded in part, C.A.D.C., No. 16583, decided June 30, 1962. The interim reduction constituted about 40 percent, on an annual basis, of the total disallowance ordered by the Commission.

return found proper by the Commission could vitiate the Commission order. Nonetheless, we deem it relevant to point out that, in our view, there was no basis for Judge Wisdom's assumption (R. 643) that the interim order "makes it highly unlikely, if not impossible" for Tennessee, during the refund period, to earn the return found proper by the Commission.²⁸

That possibility could come to pass only if Tennessee's rates as finally determined, while resulting in an overall reduction in revenue, should be above the interim rates in one or more zones. There was no reason to assume this would be the case. For, in addition to the allocation question, there still remained the question—raised by both the Commission staff and by interveners—whether other aspects of Tennessee's claimed cost of service, upon which its increased rate filing was also predicated, were not too high. At the time the Commission issued the interim order, Tennessee's increased rates were intended to yield about \$75,000,000 more in revenues than the last Commission-approved rates. Even after the interim

²⁸ Judge Wisdom observed (R. 643), for example, that "Tennessee, therefore, will be unable to earn the return the Commission considers just and reasonable, no matter what the rate is" and that " * * * the retroactive effect of the eventual determination of cost allocation makes it highly unlikely, if not impossible, for a utility to earn a 'just and reasonable return' * * *". Judge Wisdom similarly stated (R. 633) in dissenting from the denial of a requested stay, that "it is unreasonable * * * in this case, for the Commission to specify a rate of return for Tennessee * * * when at the time of issuing the order the Commission knows that there is a likelihood that the company cannot possibly realize the rate of return."

rate reduction order, this figure was still in excess of \$64,000,000. This large increase was necessarily based on substantial increases in Tennessee's estimates of various factors in its cost of service. It may be noted that the examiner, in his decision on the second phase of this case, issued on May 28, 1962, determined that Tennessee's cost of service was \$25,000,000 less than that for which it had contended.²⁹ Application of the allocation principles recently announced by the Commission in the other Tennessee case (G-11980) to the examiner's cost of service indicates that the costs allocable to each of Tennessee's six rate zones are less than the revenues Tennessee expected to obtain from it. See, *infra*, App. C, p. 62. Barring wide departure by the Commission from the examiner's cost findings, there will be reductions below the interim rates in every zone and hence no loss of any kind to Tennessee.

III. THE COLUMBIA COMPANIES ARE NOT PREJUDICED BY THE INTERIM RATE REDUCTION

An unusual facet of this case is that one group of customers, for quite different reasons from those advanced by Tennessee, suggests that it might be prejudiced—implausible though that seems on the face of it—by the *reductions* which the Commission has

²⁹ The examiner's cost of service is about \$29,000,000 less than the revenues that Tennessee expected the interim rates to generate. It should also be noted that the examiner's cost of service includes in purchased gas costs various amounts still being paid with the possibility of refunds from independent producers.

ordered in Tennessee's charges.³⁰ The Columbia companies, which purchase gas from Tennessee in some of the latter's zones of service, contend that Tennessee's allocations are highly improper and that Columbia is a victim of discrimination. Columbia then reasons as follows. The Commission could ultimately uphold Columbia's contentions as to allocations and find that Tennessee's increased rates, insofar as they involve the zones in which Columbia purchases, are highly excessive. It might also conclude that ~~the~~ the rates in certain other zones are unduly low. If these eventualities occurred, substantial refunds would be due Columbia for past periods as a result of the discrimination practiced by Tennessee. But, Columbia says, if Tennessee does not continue to collect from all of its customers sufficient revenues both (a) to provide it an over-all rate of 6 $\frac{1}{8}$ percent and (b) to make whole those customers which have been overcharged, Columbia may suffer. This argument assumes, of course, that the Commission is guaranteeing Tennessee a 6 $\frac{1}{8}$ percent rate of return for past

³⁰ In large measure, the interest of Columbia is that of a stakeholder. The three Columbia companies that are parties to this action increased their jurisdictional rates to reflect Tennessee's increased rates, and settlements with respect to each of the Columbia companies' present rates specifically provide for refunds to its customers of refunds from Tennessee for the period from April 5, 1960, on. See *Manufacturers Light and Heat Co.*, 25 F.P.C. 595, 599; *Ohio Fuel Gas Co.*, 26 F.P.C. 213, 216; *United Fuel Gas Co.*, ordered issued March 20, 1962. It is notable that consumers who receive Tennessee gas transmitted by Columbia support the Commission's interim reduction. See the briefs filed by City of Pittsburgh, petitioner in No. 50, and the Commonwealth of Pennsylvania, as *amicus curiae*.

periods, even if it should develop that Tennessee has failed, as a result of its own acts of gross discrimination, to collect from proper sources sufficient revenues to yield the designated rate of return. Putting aside the point that there appears to be no reasonable probability that this situation will ultimately be presented, there is no warrant for the assumption that the Commission would permit the victim of discrimination, rather than its perpetrator, to suffer the burden.

Columbia also appears to be of the view that the Commission's interim reduction order somehow deprives it of a hearing on the question whether Tennessee's rates in certain zones should be reduced upon grounds of discrimination. We turn first to this threshold contention.

A. The interim reduction left opportunity for hearing unimpaired on all issues other than rate of return

The claim of Columbia that it has been deprived of a hearing on the zone allocation issue seems to assume that a final determination has been made as to Tennessee's rates during the refund period. But an examination of the orders under review plainly shows that the contrary is true and that the order requiring immediate reduction of Tennessee's rates did not prejudice the allocation issues. For while the effect of the Commission order was to require Tennessee to file substitute increased rates reflecting the lower 6 $\frac{1}{8}$ percent rate of return, the substitute rates were to be in effect for the same period as the originally filed rates would have been and are subject to the same refund obligation under Section 4(c) of the Act. Spe-

cifically, the Commission in paragraph (C) of the ordering paragraph of the order under review, stated (R. 539):

(C) Upon acceptance of such filing of substitute rates as satisfactory to the Commission, the rates, charges and classifications set forth in Tennessee's substitute tariff sheets shall become effective as of April 5, 1960, subject to refund, in accordance with the Commission's order of April 29, 1960, and the undertaking heretofore filed by Tennessee, in compliance with the terms of that order, and subject to further orders of the Commission in this proceeding.

As the Commission observed (R. 536), the interim reduction order leaves Columbia in the same position as if Tennessee originally had filed increased rates based on the $6\frac{1}{8}$ percent rate of return approved by the Commission. By filing increased rates and putting them into effect subject to refund, Tennessee subjected itself to making refunds to the extent these rates should ultimately be found not justified—whether this finding results from a determination that the over-all cost of service is excessive or that the resulting rates are unduly discriminatory or preferential. The claim that Columbia has been deprived of a fair hearing on the zone allocation issue was not adopted, below and is frivolous.³¹ As Chief Judge

³¹ Contrary to the view expressed in Columbia's brief in opposition (pp. 7-8), we have found nothing in Judge Wisdom's opinion adopting the Columbia position. Indeed, his opinion clearly shows that, in setting aside the interim order, he was concerned only by the possibility of "injury" to Tennessee.

Tuttle noted (R. 645) in dissent, the Columbia companies "are undoubtedly entitled to such a determination, but not necessarily before the Commission can eliminate what it finds to be an unlawful increment in the price structure. * * *"

B. It is not necessary to continue excessively high rates in order to preserve power to correct discrimination

Columbia's argument that the interim reduction would cause it economic injury depends, in the first place, on a series of speculations and unwarranted assumptions. It assumes, of course, that the rates finally approved by the Commission will exceed the interim rates in zones where the Columbia companies are not customers of Tennessee. We have already shown that this is unlikely (*supra*, pp. 39-41). Even if the Columbia allocation methods were accepted, the prospect that any of the final rates would exceed the interim rates is conjectural at best, particularly in view of the large portion of Tennessee's cost of service which has been disallowed by the examiner. See, *supra*, p. 41.

But should these eventualities nonetheless occur, the apprehended injury to Columbia would result only if it were also correct in suggesting that Tennessee cannot, and will not, be required to make full refunds at the conclusion of the entire rate proceeding. Certainly, the Commission's determination that a 6 $\frac{1}{8}$ percent (as opposed to a 7 percent) rate of return is proper does not carry with it a guarantee that Tennessee must in all events be permitted to retain revenues affording that rate of return for the

interim period. Tennessee is entitled to charge lawful rates which will yield it a lawful rate of return. It obviously does not follow that it is entitled to collect and retain discriminatory rates merely because they yield, on the average, such a return. In short, the Commission's determination as to the permissible rate of return nowise inhibits it from directing that refunds be made to those who may have been unlawfully overcharged by reason of discrimination.

CONCLUSION

For the foregoing reasons, the judgment of the Court of Appeals should be reversed.

Respectfully submitted.

ARCHIBALD COX,

Solicitor General.

JOSEPH D. GUILFOYLE,

Acting Assistant Attorney General.

RALPH S. SPRITZER,

Assistant to the Solicitor General.

RICHARD A. SOLOMON,

General Counsel,

HOWARD E. WAHRENBROCK,

Solicitor,

PETER H. SCHIFF,

Attorney,

Federal Power Commission.

AUGUST 1962.

APPENDIX A

The Natural Gas Act of 1938, 52 Stat. 821, as amended, 15 U.S.C. 717, *et seq.*, provides, in pertinent part, as follows:

* * * * *

SEC. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification,

or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine

the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

* * * * *

SEC. 16. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this Act. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this Act; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for pub-

lie inspection and examination during reasonable business hours.

* * * * *

SEC. 19. (b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28, United States Code. Upon the filing of such petition such court shall have jurisdiction; which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive * * *

* * * * *

APPENDIX B

United States of America Federal Power Commission

Before Commissioners: Jerome K. Kuykendall,
Chairman; Frederick Stueck, William R. Connole
and Arthur Kline

Docket No. G-5259

IN THE MATTER OF TENNESSEE GAS TRANSMISSION
COMPANY

ORDER GRANTING MOTION IN PART

(Issued September 20, 1956)

By order issued on October 6, 1955, herein the Commission directed that the evidence first to be thereafter presented at further sessions of the hearing should be confined to the total cost of service of Tennessee Gas Transmission Company (Tennessee) and to the rate level. It also provided that, thereafter, the Presiding Examiner should allow such period of time as might be necessary for the preparation of evidence to be offered in connection with the zoning issue; and that the latter evidence should be presented at a separate and subsequent phase of the hearing.

Upon conclusion of the non-zoning phase of the hearing on July 19, 1956, Tennessee moved orally upon the record that the Commission:

(1) Proceed to final decision on the issues relating to total cost of service and rate level,

with an order to be issued fixing Tennessee's rates for jurisdictional sales on and after December 15, 1954 (the commencement of the refund period herein), and continuing until the effective date of any Commission order subsequently issued on the zoning question;

(2) Omit the intermediate decision procedure and fix dates for the filing of briefs on the issues as to total cost of service and rate level; and

(3) Set a date for the commencement of a separate phase of the hearing herein on the zoning issue.

Tennessee alleged in support of the motion that:

(a) This proceeding involves a rate increase filed by Tennessee on November 3, 1954, the sole purpose of which was to reimburse Tennessee for increases in the cost of gas purchased from its suppliers pursuant to effective rate schedules, which the Commission had permitted to become effective without suspension. The new rates added such increased gas-purchase costs to the settlement rates effective pursuant to the order issued September 11, 1954, in Docket No. G-2434, and, as thereafter modified, effective November 18, 1954. Tennessee proposes to obtain such reimbursement by increasing the commodity component in all sales rate schedules by 1.9¢ per Mcf.

(b) The purpose of the motion is to effectuate the provisions of the order issued October 6, 1955, by expediting a final decision on the issue of the total cost of service and rate level.

(c) The Commission is prohibited by section 5(a) of the Natural Gas Act from ordering an increase in the currently-effective rates on file with the Commission. This limitation is equally applicable to this proceeding instituted under section 4(e) of the Act. Thus, in this proceeding, the Commission's order following the phase of the hearing on the zoning issue, if the Com-

mission were to adopt new zone rate differentials which required an increase in the presently-filed rate in any zone, could not be effective for any period prior to the effective date of such order.

The motion has been certified to the Commission by the Presiding Examiner in accordance with the Commission's Rules of Practice and Procedure.

At the July 19 session of the hearing, counsel for the numerous interveners present requested an opportunity to file written answers to the motion. Because of the importance and complexity of the issues raised by the motion, the Presiding Examiner granted the request, and fixed July 30, 1956, as the termination date for the filing of answers. The Presiding Examiner afforded Tennessee opportunity until August 6, 1956, to file a reply to such answers.

Answers to the motion of Tennessee were filed by a number of interveners and Staff Counsel. Thereafter, Tennessee, on August 6, 1956, filed its reply.

The answers of the interveners, in the main, objected to the motion in its entirety. It is asserted that the Commission's authority in this proceeding is to determine after full hearings whether or not the increased rates and charges of Tennessee are unjust or unreasonable or unduly discriminatory or preferential; and, if it so finds, to determine the just and reasonable rates and charges to be thereafter observed and to fix such rates and charges by order.

As to the period preceding the date of such order, it is asserted that the Commission's authority is to direct refunds of any portion of any collected rates and charges found not justified. The Commission cannot fix a rate from December 15, 1954, onward to recover Tennessee's over-all cost of service—so the argument runs—until the Commission has considered

and passed upon the issue of zone differentials and is able to determine not only what the overall cost of service should be, but is also able to determine what are just and reasonable zone rates. It appears that the majority of the interveners fear that the motion, if granted, would deny them refunds to which they might otherwise be entitled.

All the interveners—save the Columbia Gas System companies—object to the request that the intermediate decision procedure be waived. Staff Counsel objected to the request for the omission of the intermediate decision procedure only.

In reply, Tennessee asserted that it would be inequitable and unreasonable to prescribe rates and charges and rate differentials to be effective retroactively which would be different than the historic zone differentials so as to deprive Tennessee of revenues equalling its total cost of service.

The pleadings pose the questions of whether it is appropriate and in the public interest for the Commission at this time and on the present record to consider and determine separately the issues relating to total cost of service and rate level and to reserve for subsequent decision the issue raised concerning zone rate differentials; and should the intermediate decision procedure be omitted.

At the outset of our discussion, we take note that the record is ripe for decision as to Tennessee's total cost of service for the test period. Tennessee and all other parties, including the Staff, have been fully heard on this issue. The pleadings inform us also that there are in this record several different estimates of Tennessee's cost of service. These have been presented by Tennessee, the Staff, and a group of interveners.

We take particular note also of the fact that none of the parties appears to suggest that the Commission or the Presiding Examiner—if the intermediate decision procedure is not waived—may not in the present posture of the proceeding proceed to a decision upon the total cost of service. To the contrary, certain of the interveners urge that a decision now be made on this point.

Decision at this time as to Tennessee's cost of service would apprise all parties of the proper costs to be allocated. Accordingly, such a decision now should facilitate preparation of evidence to be presented in the further hearings to be had herein on the zoning issue. It would avoid presentations on different bases by different parties and should tend to simplify and shorten the record on the issues remaining to be heard. All of which should serve to expedite the hearing and decision on the zoning issue.

In consideration of the foregoing and in the particular circumstances of this case, we conclude that Tennessee's motion should be granted to the extent that it requests a determination now as to its proper total cost of service for the test period.

Resolution of the question of whether it is appropriate and in the public interest for us at this time and on the present record also to consider and determine separately the issue relating to rate level (i.e., to fix Tennessee's rates from December 15, 1954) and to reserve for subsequent decision the issue raised respecting zone rate differentials presents more difficulty. In this connection, we note that in the order issued herein on October 6, 1955 we found "that the question of possible unlawful rates between zones is a relevant issue in a rate proceeding." There, we said that:

The zone boundaries and rate differentials between the zones served by Tennessee have not been prescribed by a Commission order but have been carried only in the rate schedules filed by Tennessee. In a system as complex as that operated by Tennessee the charges of unjustness in the rates as between zones require a thorough and exhaustive study to determine proper zone boundaries and what method of allocating costs between zones would be fair and equitable to all concerned; in order that just and reasonable rates may be prescribed for each zone.

By reason of the peculiar circumstances in the present case, the question of zone rates may reasonably be separated for hearing purposes from the question of the cost of service involved in the balance of this rate proceeding. It seems appropriate, therefore, to separate the zoning issue from the pending rate proceeding, allowing the interested parties sufficient time to prepare the evidence in the zoning case.

Accordingly, the order provided for a date for resumption of the hearing—

at which time the testimony and evidence shall be confined to the question of cost of service to the Tennessee Gas Transmission Company as a whole and the rate level. Upon the conclusion of the testimony with respect to the cost of service and the rate level, the Examiner should allow such period as may be necessary for the preparation of evidence respecting the reasonableness of the suspended rates which are involved in this proceeding.

The order issued October 6, 1955, conjunctively refers to the cost of service "as a whole and the rate level." Similarly, the motion of Tennessee refers to "total cost of service and the rate level." Since Tennessee is engaged in rendering jurisdictional and non-jurisdictional service, it is not possible to translate

the "total" of Tennessee's cost of service into jurisdictional "rate level" without first determining the portion of the "total" properly allocable to jurisdictional sales. Accordingly, even though we find that it is now appropriate to determine the "total" of Tennessee's cost of service, such cost of service cannot be translated into jurisdictional rates (or "rate level") until decision is made as to the proper method of allocating the "total" between jurisdictional and non-jurisdictional sales.

Fulfillment of the request of Tennessee that determination be now made as to its total cost of service and the rate level would not only require determination as to the proper method of allocating the "total" between jurisdictional and non-jurisdictional sales, but it would require also present determination as to the proper method of allocating the jurisdictional portion of the "total" between the several zones of service, or, at least, a determination that the present zone boundaries and rate differentials should be maintained for sales made on and since December 15, 1954, and continuing until final order in this proceeding. It is not possible at this incomplete state of the proceeding to determine proper zone boundaries and what method of allocating costs between zones would be fair and equitable.

As we said in the order of October 6, 1955, the prescription of just and reasonable rates for each zone requires "a thorough and exhaustive study to determine proper zone boundaries and what method of allocating costs between zones would be fair and equitable to all concerned." Only the New England interveners have been allowed to present evidence on the zoning issues; and this evidence has yet to be subjected to cross-examination. Other interveners and

the Staff will be afforded an opportunity to present such evidence in the next phase of the hearing.

Moreover, our experience tells us that, if in the future a change in Tennessee's zone boundaries or rate differentials is in order, the effect of the resultant rate on particular customers will differ dependent upon what cost of service is found proper here. On this record, however, it is not possible to now determine what the effect upon particular customers will be until resolution of the cost of service and zone issues.

Thus, we are of the opinion that it would be not only premature for us to grant that part of Tennessee's motion requesting that we at this time fix rates to be effective on and after December 15, 1954, it would also be unfair and improper.

Not having the record before us, we, of course, cannot determine now what the proper decision should be as to Tennessee's total cost of service for the test period. We have concluded that this is a decision to be made by the Presiding Examiner, because we deem it necessary to a proper exercise of the Commission's function in this case that the Presiding Examiner—who has heard the case and had opportunity to evaluate fully the testimony—render an initial decision upon this point prior to any undertaking of the Commission to pass upon this aspect of the matter. It appears that the transcript of testimony exceeds 3,000 pages and that many exhibits have been introduced. The issues raised are quite complex and technical. Under these circumstances, the initial decision of the Presiding Examiner upon the issue respecting total cost of service would be helpful, not only to the Commission, but also to the parties. Accordingly, we shall deny Tennessee's instant request that the intermediate procedure be omitted so far as the non-zoning aspects of the case are involved.

In view of the foregoing, we further conclude that the Presiding Examiner, consistent with the opinions and conclusions herein expressed, should forthwith determine on the basis of the present record the total cost of service of Tennessee for the test period.

The Commission finds:

(1) It is appropriate and necessary in the public interest and for carrying out the provisions of the Natural Gas Act that the aforesaid motion of Tennessee be granted to the extent only that it requests that a determination be now made as to Tennessee's total cost of service.

(2) It is appropriate and necessary in the public interest and for carrying out the provisions of the Natural Gas Act that the aforesaid motion of Tennessee be denied to the extent that it also requests the present determination and fixing of the rates to be effective for jurisdictional sales made on and after December 17, 1954 and, continuing until the effective date of any Commission order subsequently issued on the zoning question.

(3) The Commission is unable to find that its functions imperatively and unavoidably require the omission of the intermediate decision procedure upon the non-zoning phase of this proceeding.

The Commission orders:

(A) Upon the expiration of the time hereinafter provided for the filing of briefs by the parties to this proceeding, the Presiding Examiner, consistent with the findings and conclusions herein set forth, shall forthwith determine Tennessee's total cost of service for the test period.

(B) Initial briefs of all parties upon the issue respecting Tennessee's cost of service for the test period, including the Commission's

Staff, shall be filed within 30 days from the date of issuance of this order; and reply briefs shall be filed within 45 days from the date of issuance of this order.

(C) Except to the extent granted in paragraph (A) above, the motion of Tennessee be and it is hereby denied.

(D) Upon the issuance of the decision contemplated by paragraph (A) above, the Presiding Examiner shall fix a date for further hearings herein concerning the issues raised as to matters other than the total cost of service of Tennessee for the test period.

By the Commission. Commissioner Comole not participating.

Leon M. Fuquay,
LEON M. FUQUAY,

Secretary.

APPENDIX C

The following shows (1) the revenues Tennessee estimated its interim rates would yield in each of its six rate zones for jurisdictional sales and (2) the cost of service for each of these zones determined by our applying the allocation principles announced by the Commission in the Opinion in F.P.C. Docket No. G-11980 (*Tennessee Gas Transmission Co.*, decided February 6, 1962, 42 P.U.R. 2d 145) to the cost of service determined by the examiner in the second phase of this case (*Tennessee Gas Transmission Co.*, F.P.C. Docket No. G-10983, decision issued May 28, 1962).

Sales	Revenues at Interim Rates	Allocated Costs
Southern Zone.....	\$32,335,232	\$28,833,190
Central Zone.....	21,698,723	19,413,150
Eastern Zone.....	78,927,166	70,219,997
Northern Zone.....	57,110,143	50,557,409
New York Zone.....	43,185,923	38,514,783
New England Zone.....	32,937,267	30,908,385
Total.....	266,194,454	238,446,914

FILED
AUG 23 1962

JOHN F. DAVIS, CLERK

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1962

No. 50

CITY OF PITTSBURGH, PENNSYLVANIA,
Petitioner,

v.

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT & HEAT
CO., THE OHIO FUEL GAS COMPANY, and
UNITED FUEL GAS COMPANY,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF
APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE CITY OF PITTSBURGH,
PENNSYLVANIA

DAVID W. CRAIG,
*City Solicitor,
City of Pittsburgh,
Pennsylvania.*

CHARLES S. RHYNE,
EDWARD D. MEANS, JR.,
*Rhyns & Rhync,
400 Hill Building
Washington 6, D. C.
Attorneys for Petitioner,
City of Pittsburgh, Pennsylvania.*

INDEX

	Page
Opinions Below	1
Jurisdiction	1
Question Presented	2
Statute Involved	2
Statement	2
Pittsburgh's Relation To The Controversy	2
The Proceedings Before The Commission	3
The Proceedings Before The Fifth Circuit	7
Summary of Argument	8
Argument	15
I. The Importance Of The Interim Order Procedure In The Protection Of The Consumer	15
II. The Authority Of The Commission To Use The Interim Order Procedure and The Judicial Support For It	19
III. The Fifth Circuit Erroneously Limited The Commission's Rate Powers	23
A. A Pending Zone Allocation Issue Does Not Deprive The Commission Of The Interim Order Procedure	24
B. The Fifth Circuit Erred In Concluding That The Allocation Issue Was Ripe For Decision	27
IV. Refunds Are Not An Adequate Substitute For The Interim Order Procedure In Protecting The Consumer	28
Conclusion	30

CITATIONS

Cases:

<i>Federal Power Commission v. Hope Natural Gas Company</i> , 320 U.S. 591	9, 15, 17
<i>Federal Power Commission v. Natural Gas Pipeline Company</i> , 315 U.S. 575	9, 20
<i>Illinois Commerce Commission v. Natural Gas Pipe Line Company of America</i> , 2 F.P.C. 218	21

<i>Panhandle Eastern Pipeline Company v. Federal Power Commission</i> , 236 F. 2d 606	21, 22, 26
<i>State Corporation Commission of Kansas v. Federal Power Commission</i> , 206 F. 2d 690, certiorari denied 346 U.S. 922	22, 26
<i>Tennessee Gas Transmission Company v. Federal Power Commission</i> , 283 F. 2d 729	7
<i>Tennessee Gas Transmission Co.</i> , decided February 6, 1962, 42 P. U. R. 3d 145, pending on review sub nom. <i>Manufacturers Light and Heat Company v. Federal Power Commission</i> , C. A. D. C. No. 17064	27
<i>Tennessee Gas Transmission Co.</i> , Docket No. G-19983, Examiner's decision issued May 28, 1962 (unreported)	7, 17
<i>Tennessee Gas Transmission Company</i> , 18 F.P.C. 428	4
<i>United Gas Pipeline Company v. Memphis Light, Gas and Water Division</i> , 385 U.S. 103	16
<i>United Gas Pipe Line Company v. Mobile Gas Service Corporation</i> , 350 U.S. 332	16

Statutes:

Natural Gas Act, June 21, 1938, c 556, 52 Stat. 821-833, as amended, 15 U.S.C. 717-717w	2, 8, 9, 10 11, 13, 14, 15, 16, 17, 19, 20 22, 25, 27, 28, 29
Section 4, 15 U.S.C. 717c	19
Section 4(a), 15 U.S.C. 717c(a)	15
Section 4(d), 15 U.S.C. 717c(d)	3
Section 4(e), 15 U.S.C. 717c(e)	16, 17, 19, 24
Section 5, 15 U.S.C. 717d	19
Section 5(a), 15 U.S.C. 717d(a)	20
Section 16, 15 U.S.C. 717o	11, 19, 20

Miscellaneous:

House Report 2651, 74th Cong., 2nd Sess.	15
House Report 709, 75th Cong., 1st Sess., pp. 1-3	15
Senate Report 1162, 75th Cong., 1st Sess.	15
81 Cong. Rec. 6721-6728	15

IN THE
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1962

No. 50

CITY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

TENNESSEE GAS TRANSMISSION COMPANY,
THE MANUFACTURERS LIGHT & HEAT
CO., THE OHIO FUEL GAS COMPANY, and
UNITED FUEL GAS COMPANY,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF
APPEALS FOR THE FIFTH CIRCUIT

**BRIEF FOR THE CITY OF PITTSBURGH,
PENNSYLVANIA**

Opinions Below

The orders of the Federal Power Commission (R. 524-540; 585-591) are reported at 24 F.P.C. 204 and 525. The opinions of the United States Court of Appeals for the Fifth Circuit (R. 635-646) are reported at 293 F.2d 761.

Jurisdiction

The judgment of the Court of Appeals setting aside the Federal Power Commission's order was entered

on August 2, 1961. A petition for rehearing, timely filed by the Commission, was denied on October 5, 1961. The petition for writ of certiorari was filed December 11, 1961, and granted on January 22, 1962 (R. 660), 368 U.S. 974. The jurisdiction of this Court rests upon 28 USC 1254, and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

Question Presented

Where the Federal Power Commission, after full hearing, finds that a pipeline company has filed increased rates which are unlawful in part because they are based upon a 7% rate of return when the lawful rate is 6 $\frac{1}{8}$ %, may the Commission order an immediate rate reduction of $\frac{7}{8}$ % or must consumers continue to pay at the 7% rate for approximately another two years until other issues involved in the increased rate filing are all finally resolved by the Commission?

Statute Involved

The pertinent provisions of the National Gas Act, 52 Stat. 821-823, as amended, 15 U.S.C. 717-717w, are set forth in Appendix A of the Brief for the Federal Power Commission in Companion case No. 48 (at pp. 47-51 thereof).

Statement

Pittsburgh's Interest In the Controversy

The City of Pittsburgh, Pennsylvania (Pittsburgh) has approximately 600,000 residents, most of whom are ultimate consumers of natural gas. Tennessee Gas Transmission Company (Tennessee), a natural gas interstate pipeline company, sells large quantities of natural gas to the Pittsburgh area distributor com-

panies, viz., The Manufacturers Light and Heat Company (one of the respondent Columbia Companies), Peoples Natural Gas Company, and Equitable Gas Company, who resell gas to Pittsburgh and its residents as ultimate consumers of natural gas.

Pittsburgh was a party in the rate proceedings before the Commission and before the Court of Appeals as a consumer and as a representative of its resident consumers. The increased rates charged by Tennessee to the distributors have been passed on to and are being paid by these consumers. The Commission's interim order of August 9, 1960, which is involved here, benefits consumers in Pittsburgh by creating lower rates and providing refunds of the excess unlawful charges to these consumers. In total dollars, Tennessee's annual increase in this rate proceeding was reduced from approximately \$75 million to \$64 million as a result of the Commission's determination of a 6½% rate of return and the interim rate reduction which followed.

The Proceedings Before The Commission

This controversy arises out of an increased rate filed by Tennessee on October 5, 1959¹ pursuant to Section 4(d) of the Natural Gas Act. This rate increase filing represents an annual increase of \$26,590,138 in Tennessee's revenues based on sales for the year ended July 31, 1959. This is the third in a series of pending, contested and undisposed of annual increases in rates filed by Tennessee. In 1957, Tennessee filed an approximate \$24 million annual rate increase (Docket No. 11980), and in 1958 an approximate \$20 million annual

¹Commission Docket No. G-19983.

rate increase (Docket No. G-17166). These increases became effective, and have been collected as filed subject to refund since July 14, 1957 and May 15, 1959, respectively. Together, these three increases represent a pyramiding of approximately \$75 million annually in increased rates.² This increased rate was predicted on a claimed cost of service which included a 7% rate of return on net investment (R. 490-501).³

On November 4, 1959, the Commission issued an order providing for a hearing to determine the lawfulness of the new rates herein involved and suspended their operation for the statutory maximum period of five months (R. 502-505). The hearing commenced February 2, 1960 (R. 524). The five month suspension period ended on April 5, 1960. During the course of the hearing the rates became effective subject to Tennessee's obligation to refund any amount found by the Commission to be unjust and unreasonable (R. 505-509).

At the hearing, Tennessee presented all of its direct evidence, but its witnesses were cross-examined only on the issue of rate of return. The staff of the Federal Power Commission and one intervenor, West Virginia Public Service Commission, presented evidence on rate of return only, and their witnesses were cross-examined. Tennessee presented rebuttal testimony on

² See Footnote 1, Page 3 of the Federal Power Commission's brief in No. 48 for an explanation of how this \$75 million figure is derived.

³ The rate of return last approved by the Commission for Tennessee before then had been 6% in 1957, 18 F.P.C. 428. In Docket Nos. G-11980 and G-17166, the rates of return used by Tennessee were less than 7% but more than the 6 1/4% which the Commission subsequently found to be reasonable in Docket No. G-19983.

rate of return and cross-examination of this testimony was completed May 25, 1960 (R. 524-525):

When the taking of evidence on rate of return had been concluded, the Commission staff counsel moved that the proceeding be divided into two parts:

(1) Determination of the rate of return by the Commission directly, with omission of the Hearing Examiner's intermediate decision. He further proposed that if a proper rate of return was less than 7%, the Commission should enter an interim order reducing Tennessee's rates to the extent of the reduced amount and directing corresponding refunds for the past.

(2) Determination of the other elements entering into Tennessee's cost of service following the usual procedure (including the Presiding Examiner's intermediate decision) (R. 525).

While omission of the Examiner's intermediate decision on rate of return was unopposed (R. 513), Tennessee opposed the interim order procedure.⁴ Tennessee relied upon the fact that the proper method of allocating its cost of service among its six zones was in dispute, and that in the pending first rate increase for an earlier period of time, Docket No. G-11980, the zone allocation issue had been tried and was awaiting decision by the Hearing Examiner⁵ (R. 591-606).

⁴ Several other intervenors, including the Columbia Companies, the other respondents here, also opposed the interim order procedure (R. 607-625).

⁵ The Examiner indicated that the determination of the zone allocation issue in Docket No. G-11980 would be similarly applied in the current docket.

On June 17, 1960, the Commission granted the motion to omit the Examiner's intermediate decision on the rate of return, and provided for oral argument on the merits of the rate of return and on the procedure of ordering interim rate reductions and refunds if 7% was found excessive (R. 513-516). On June 19, 1960, Tennessee, by motion, requested the Commission to waive the intermediate decision procedure on the zone allocation issue in Docket No. G-11980 and to decide that issue simultaneously with the rate of return issue in this proceeding (Docket No. G-19983) (R. 519-521). On August 5, 1960, the Commission denied Tennessee's untimely motion (R. 521-523).

On August 9, 1960, the Commission issued the order involved here, and determined that an overall rate of return of $6\frac{1}{8}\%$ was fair, just and reasonable for Tennessee. The order disallowed the rates computed at 7%, directed Tennessee to file interim reduced rates (subject to possible further refund at the end of the entire case) effective April 5, 1960, when the originally filed rates went into effect, and ordered Tennessee to make refunds from that date for any sums collected in excess of the interim reduced rates (R. 526-540). The Commission held that by requiring Tennessee to substitute rates founded on a proper rate of return, but otherwise using Tennessee's own filed rates, Tennessee and its customers were put in the same position as if Tennessee had originally filed increased rates on a lawful rate of return.

On September 27, 1960, the Commission denied an application for rehearing by Tennessee and the Columbia Companies (R. 585-591). Both applications attacked the interim order procedure, and Tennessee challenged the decision awarding a $6\frac{1}{8}\%$ rate of return. The Commission pointed out that the order of August

7
9 providing for the filing of lower rates based on the 6¹/₈% return would result in a savings to Tennessee's jurisdictional customers of approximately \$11 million annually. The substitute filing, made in November 1960, has resulted in an annual revenue reduction, in relation to "test year" figures, of about \$11 million.⁶ Tennessee has refunded \$7,416,663, plus interest, for the period from April 5, 1960, through October 31, 1960.⁷

The Proceedings Before The Fifth Circuit

The Court below unanimously affirmed the Commission's determination that 6¹/₈% was a just and reasonable rate of return for Tennessee.

In regard to the interim order procedure, however, the Court set aside the Commission order by a 2 to 1 vote, Chief Judge Tuttle dissenting and Circuit Judge Cameron concurring in the result only, to the extent that it required Tennessee to make immediate refunds, and to make lower rates effective immediately. The majority opinion held (1) that the lack of a Commission decision on cost allocation by zones meant there was no basis for determining which of the filed rates in specific zones were lawful; (2) that while the allocation of costs in all the schedules was made by Tennessee and the burden rests on it to justify each rate in-

⁶ Stays of the reduction and refund were denied by the Fifth Circuit, Judge Wisdom dissenting, *Tennessee Gas Transmission Co. v. Federal Power Commission*, 283 F.2d 729 (C.A. 5).

⁷ On the basis of other issues pending in Docket No. G-19983, the Examiner recently issued a decision disallowing about \$26,000,000 of the cost of service claimed by Tennessee in addition to the \$11 million disallowed here. *Tennessee Gas Transmission Co., F.P.C.* Docket No. G-19983, decision issued May 28, 1962.

crease, Tennessee should not be held at its peril to foretell the decision of the Commission on the correctness of the increased rates; (3) that, until the Commission fixes the rates, the Company is protected by being allowed to collect at the filed rate and the consumer is protected by the Company's obligation to refund any excess charges with interest; and (4) regardless of the Commission's authority to issue the order, the cost allocation among zones is such an essential element in determining whether filed rates are excessive that it was an abuse of discretion to issue an interim order before deciding the allocation issue (R. 643).

Chief Judge Tuttle, dissenting, declared that he would have affirmed the Commission's order giving immediate effect to the conclusion that the rates based on the excessive rate of return were unreasonable. In his view, under the Natural Gas Act, Tennessee has the burden of establishing the validity of each element in its rate increase filing, including the cost allocations which it makes; and Tennessee cannot complain if it is placed, by the Commission's order, in the position it would have occupied initially had it based its rates on a proper rate of return (R. 646).

On October 5, 1961, the same panel of the Court, Chief Judge Tuttle again dissenting, denied the Commission's petition for rehearing *en banc*.

Summary of Argument

This case involves an interim rate procedure adopted by the Federal Power Commission to remedy an evil flowing from the practice whereby natural gas pipeline companies file and collect from consumers grossly excessive rates. This interim rate procedure carries out the often declared purpose of the Natural Gas Act to pro-

protect consumers against unlawful exploitation by pipeline companies. The decision below erroneously rejects this purpose. It bases its reversal of the Commission upon a newly found purpose of protecting pipeline companies against possible or speculative pipeline company errors. The decision below has as its fundamental foundation, the erroneous assumption that the Natural Gas Act requires consumers to put up large enough amounts of money, even when unlawfully extracted, to guarantee or insure pipeline companies against their own possible errors in rate design. Such a decision is clearly wrong, and it must be reversed when the provisions of the Natural Gas Act are applied to the facts in this case.

The decision of the Court below, by setting aside this interim rate of return order, has impaired the continued ability of the Commission to use this important procedural device for curbing, at least to some extent, unjustified rate increases and collections of excess rates by interstate natural gas companies from customer purchasers and consumers of natural gas. The decision is in conflict with decisions of the Third and Eighth Circuits, and is inconsistent with the views of this Court in *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U. S. 575, 583-585.

1. This Court has declared that the primary purpose of the Natural Gas Act is "to protect the consumer interests against exploitation at the hands of private natural gas companies," *Federal Power Commission v. Hope Natural Gas Company* 320 U. S. 591, 612. "In keeping with this primary purpose, the interim order procedure provides the Commission with an effective means of providing consumers with a direct, and an immediate, remedy as a deterrent to the constant prac-

tice of interstate pipeline companies of grossly overstating their rate claims so as to collect for their use unwarranted amounts from consumers. At the same time, the interim procedure fully protects the company's right to a complete hearing and determination of all other controverted and complex issues. The interim order procedure must be upheld or the Commission must stand helplessly by during the pendency of lengthy and complex rate increase cases and permit the unjustified collection of tremendous amounts in excess rates from customers and consumers. This helplessness will exist in cases where as here the unlawful excess is beyond question and to allow its collection is a clear unjustifiable exploitation of consumers.

II. Under the statutory scheme of the Natural Gas Act, the seller of natural gas initiates rates and rate changes which are then subject to Commission review. The seller has the burden of proof in justifying these increases. Although this burden of proof may tend to discourage the filing of excessive rate increases, it is unfortunate for the consumer that this burden of proof is put to a test months and sometimes years after the increases go into effect rather than before. The express duty of the Commission is to decide rate increase questions as speedily as possible, and the fundamental duty of the Commission under the Natural Gas Act is to protect consumers from the burden of paying excessive rates. Under the broad rule making and ordering powers of the Natural Gas Act, the Commission is required to adopt procedures to expedite the proof, justification and correction of rate increase filings. This power and duty includes the early separate treatment and decision of issues which lend themselves immediately to such handling. And it includes the duty to

immediately order reduction of rates found to be excessive.

The rate of return issue decided in this case, is an outstanding example of a separable issue which can receive early treatment. At the time the Commission determined that a 7% rate of return on investment was excessive and that not more than 6½% could be justified, a difference of \$11 million annually, it was obvious that the many other complex issues in the case could not be disposed of until many months later. Therefore, to allow consumers to continue to pay unlawful rates based on the excessive claims of Tennessee would be a gross violation of the Commission's statutory duties. The Commission properly issued the interim reduction order to afford immediate relief to the consumers as required by the Natural Gas Act.

The Commission's rate powers are not merely limited to making ultimate determinations of just and reasonable rates. Section 16 of the Act gives the Commission power "to perform any and all acts, and to prescribe, issue, make, amend and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this Act." This Court has upheld an interim order where the company's proof did not support the rate increases it had sought with respect to certain items of the company's proposed cost of service, *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U. S. 515, 583-585. Furthermore, the five month suspension period provided for in the Act, demonstrates that Congress did not regard the refund provision as complete protection for the consumer. If Congress had concluded that refunds were a complete consumer protection it would have provided that all rates become immediately effective upon filing.

III. The Fifth Circuit erroneously took a narrow view of the Commission's rate powers when it concluded that the decision of the rate of return issue, by an interim reduction order, was an abuse of discretion when made effective before the allocation issue was decided. The decision of the majority of the Court below fails to give appropriate weight to both the initial rate making capacity of the pipeline company, and the ultimate burden of proof. Tennessee, in keeping with the concept of the Act, put together the various components constituting a cost of service upon which it based its increased rates, put the rates into effect, and then presented its justification for its actions in the hearing before the Commission. When it struck down the unlawful rate of return, the Commission allowed each other element of Tennessee's cost of service as presented by Tennessee including the zone allocations devised by Tennessee, to remain in effect. Under these circumstances the pipeline company has no valid grounds for complaint.

A. The fact that a zone allocation issue is still pending does not in any manner restrict the Commission's authority to order an immediate rate reduction after it has determined that the pipeline company failed to justify its proposed rate of return and accordingly adjusted it downward to reflect its justness and reasonableness. Tennessee argues that they may be unable to recoup for the refund period all of the revenues necessary to yield a $6\frac{1}{8}\%$ rate of return. However, this contention does not justify delaying the filing of revised rates which will provide that return. The mere possibility that Tennessee might not be able to obtain all the revenues to which it is entitled does not result from the interim rate reduction order of the Commis-

sion. This possibility could also occur without an interim rate reduction if it were determined at the conclusion of the entire case that Tennessee was entitled to more than the filed rates in some zones but required to make full refunds in other zones. Also, Tennessee cannot complain that it has a greater risk now than if it had originally filed rates based on a proper and just rate of return. In any event, the consumer is not obligated to insure a natural gas company against the effects of discriminatory rates filed by the Company or against all losses. The risks of the natural gas pipeline business are for the pipeline stockholder, not the consumer. It is enough that the pipeline company is given a monopoly market—an insured guaranteed return is not also envisioned under the Natural Gas Act.

B. The Fifth Circuit made a factual error in concluding that the allocation issue was "ripe for decision," when the interim order was adopted by the Commission. In contrast to other types of issues, rate of return requires no extensive field investigation by the Commission staff, and it presents a repetitive broad judgment question on the cost or value of capital with which the Commission is quite familiar without being materially aided sometimes by a hearing examiner's decision. However, the allocation issue discussed by the Court below, as well as other issues, present problems of novelty requiring extensive staff field investigation which not only takes longer to develop, but are of a nature that the Commission's consideration of them is enhanced by a hearing examiner's decision. The Commission's interim rate reduction order was therefore a proper exercise of its discretion. When the Commission issued the interim rate reduction order it was not in a position to decide the zone allocation

issue. This is shown by the fact that the ultimate disposition of this issue required an additional eighteen months after the Commission adopted the interim order. Therefore, the Court below erred in concluding that the zone allocation issue was "ripe for decision" when the interim order was adopted.

IV. The Court below erroneously assumed that the consumers, who continue to pay the excessive rate of return, are amply protected by the obligation of the pipeline company to refund the excess charges with interest. Unfortunately, for the ordinary householder, in contrast to the initial payment of a lower rate and holding the line against cost-of-living increases, the overpayment and refund process is a poor substitute for an immediate rate reduction. The protection to consumers given by the refund provision of the Natural Gas Act is far from adequate. Resident consumers are ambulatory, and in the years between the excess collection and the usual refund, the consumer population for given areas invariably shifts. The administering of a refund at the consumer level is therefore not only something in the nature of an approximation, but also involves administrative detail and expense which comes out of and reduces the refund. The consumer pays all these expenses and never gets all his money back. The larger the fund the greater the expense loaded onto the consumer. The pipeline company pays nothing. It is extremely unfair to require consumers to pay out money unlawfully on rate of return on the pretext that the pipeline company may have erred in the other components of the increased rate it seeks—this unlawfully collected money to be used to insure or guarantee the pipeline company against loss due to its errors.

This speculation by the Court of Appeals is contrary to both reason and experience and also contrary to the Natural Gas Act. It is not proper foundation for continued extraction of an unlawful rate of return from consumers. The Court's attempt to shift the risks of the pipeline business from pipeline shareholders to consumers finds no basis in the Natural Gas Act.

ARGUMENT

I. The Importance of The Interim Order Procedure In The Protection of The Consumer

This Court has declared that the primary objective of the Congress in enacting the Natural Gas Act is the protection of the ultimate consumer.⁹ The interest of the average consumer is in the maintenance of adequate service at a just and reasonable retail rate. It is apparent that the rate at which the consumer purchases natural gas from his local distributing company is directly related to the price at which the latter purchases from the pipeline company. In fact, the most important item in the composition of the retail rate is the wholesale rate to the distributing company, over which the Commission has jurisdiction. Section 4(a) of the Natural Gas Act requires rates and charges of natural gas to be just and reasonable, and any rate or charge that is not just and reasonable is declared unlawful. Although the interests of the consumer are

⁸ 52 Stat. 821 (1938), 15 U.S.C. § 717 et seq.

⁹ *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591. See also H. Rept. 709, 75th Cong., 1st Sess., pp 1-3 (1937); H. Rept. 2651, 74th Cong., 2nd Sess., (1936); S. Rept. 1162, 75th Cong., 1st Sess., (1937); 81 Cong. Rec. 6721-6728.

indirectly served, he is not fully protected under the Natural Gas Act. This is true because pursuant to Section 4(e) of the Act, the procedure is for a pipeline company to file new rates, charges, classifications or service charges with the Commission. In the first instance, the companies are in a position to put rate increases into effect without any dollar limitation or other measurable criteria.¹⁰ The Commission may then order a hearing to determine the lawfulness of the new rate and suspend said rate for a period of five months. At the end of the five-month period, the new rates become effective subject to refund. Hence, the consumer commences paying the new rate at the end of the suspension period and continues to pay this rate unless and until the Commission determines that the pipeline company's new rate filing is lawful or unlawful. If the rate is unlawful refunds from overcharges under the new rate filing are ordered. As a practical matter, from the time the new rate is filed to the time the Commission ultimately disposes of the issues after a full hearing, takes a considerable length of time, often a period of years, during which time the company is collecting the full amount of the new and unapproved rate from the customer and consumer. A good illustration of this fact is the proceeding before the Commission out of which this controversy arose. In Docket No. G-19983, Tennessee tendered increased rates for filing on October 5, 1959 which became effective on April 5, 1960. Since April 5, 1960, Tennessee, under its new and still unapproved rate filing, has been collecting from the customers and consumers an amount

¹⁰ *United Gas Pipe Line Company v. Memphis Light, Gas and Water Division*, 385 U.S. 103; *United Gas Pipe Line Company v. Mobile Gas Service Corporation*, 350 U.S. 332.

of \$64 million annually.¹¹ A further practical aspect which arises from the procedure of filing for new rates is the pyramiding of rate increase filings by the same company for succeeding years while the initial rate increase filing is still pending at the Commission. Thus, the sums collected from consumers subject to refund could conceivably be multiplied several times over.¹² This pyramiding of rate increase filings along with the overwhelming increases in new rate filing by all of the pipeline companies, in general, has caused a tremendous backlog of cases pending before the Commission which has brought about the so-called regulatory lag.

In an effort to extract itself from this backlog and expedite the disposition of pipeline supplier cases, the Commission has utilized, where appropriate, the interim order procedure. In keeping with the primary purpose of the Natural Gas Act "to protect the consumer interest against exploitation at the hands of private natural gas companies," *Federal Power Commission v. Hope Natural Gas Company*, 320 U. S. 591, 612, and to decide rate cases "as speedily as possible" (§ 4(e)), the interim order procedure may serve both as a direct protection for consumers and as a deterrent to the interstate pipeline companies against their practice of flagrantly overstating rate claims and the col-

¹¹ This figure of \$64 million reflects a downward adjustment of \$11 million from \$75 million as a result of the Commission's disallowance of a 7% rate of return and a determination of a 6½%. Moreover, see note 7, *supra*, where if the Commission adopts the Examiner's decision, an additional \$26 million will be disallowed from Tennessee's cost of service and will constitute excessive rates being collected from the customers and consumers.

¹² See *supra*, page 3.

lection of unwarranted increases. The very existence (and validity) of the interim order procedure as a potential remedy, utilized where appropriate, is most important to discourage the filing of exaggerated claims and rates based thereon. As used, and if upheld in this case, it demonstrates that the Commission need not and will not stand by during the pendency of lengthy rate increase cases and permit the unjustified collection of huge sums in excess rates from consumers, where some of the issues upon which the increases rest are subject to early separable examination and the justification is found to be deficient.

Moreover, the obligation of the pipeline company to ultimately refund with interest any sums found excessive is not a deterrent to filing for unreasonable increases, apparently because of the tremendous amount of capital involuntarily provided by the ratepayer at a worth exceeding the actual cost to the company. If treated as equity capital, these funds earn a much higher rate of return than their cost, for while the company makes refunds with 7% interest it recoups a large part of the interest (about half if the company is in the 52% bracket) as an income tax deduction. On the other hand, as noted hereinafter, the ultimate refund is not an adequate recompense to the ultimate ratepayer for the use of his money in contrast to the initial payment of lower rates.

Therefore, the interim order procedure is an important device in protecting the consumer who bears the burden of excessive rates. And while this device affords protection to the consumer, it does not discriminate or impose an unjust burden on the company for it places the company in the same position as it would have been had its rate filing been just and reasonable

in the first instance. The company has the burden of proof initially to justify its rate filing and having failed to meet this burden of proof it is within the discretion of the Commission as to how to afford adequate protection of the consumer in carrying out the ultimate objective of the Act. The efforts of the Commission to afford prompt relief to consumers of natural gas is of such importance that to fail to use the interim order procedure in cases like this would be a departure from the Commission's responsibility and duty in carrying out the intent of Congress and the purpose of the Natural Gas Act.

II. The Authority of The Commission To Use The Interim Order Procedure and The Judicial Support For It

The Fifth Circuit's decision makes uncertain the Commission's authority to issue an interim order and the legality of such an order when zone allocation issues are still pending. The opinion of that Court raises the question as to the circumstances under which the Commission would be justified in issuing an interim rate order.

The Commission's authority to issue interim rate orders is contained in Sections 4, 5 and 16 of the Natural Gas Act. Section 4(e) states in part as follows;

"... after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. . . . Where increased rates or charges are thus made effective, the Commission may, by order . . . upon the completion of the hearing and decision [to] order such natural gas company to refund.

with interest, the portion of such increased rates or charges by its decision found not justified."

Section 5(a) states in part as follows:

"... the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates."

Section 16 provides:

"The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules and regulations as it may find necessary or appropriate to carry out the provisions of this act."

Thus, the most cursory reading of the Act, in the light of its broad purposes, indicates conclusively that the Commission can grant relief to the consumers through the interim order device, and the act forcibly emphasizes the duty of the Commission to grant such relief when, as in the instant case, from a factual standpoint, the record is ripe for the application of the express provisions of the act.

The view of the Fifth Circuit is not consonant with the views of this Court expressed in *Federal Power Commission v. Natural Gas Pipeline Company*, 315 U.S. 575, 583-585 where this Court upheld an interim order (in a Section 5(a) rate investigation) reducing rates. This Court recognized as appropriate the two-step procedure of first "adjustment of the general revenue level to the demands of a fair return," and second, "adjustment of a rate schedule conforming to that level so as to eliminate discriminations and unfair-

ness from its details. In sustaining the interim order, this Court held that the companies were not hurt because the Commission had entered the order on the basis only of the companies' presentation of testimony, without cross-examination of such testimony or testimony by Commission witnesses, 315 U.S. at 584, a situation much less complete than the instant case where the entire testimony and cross-examination was submitted on both sides of the issue covered by the interim order.

The basis and justification for issuing an interim order is made clear in the following language of the Commission:

"There are those who will be rendered unhappy by the frustration of their ambition to maintain the excessive rates presently charged by the defendant-respondent companies. But to refuse a substantial reduction thereof would require us to sit aloof from reality, and permit unlawful rates to exist without affording those suffering thereby any relief. Inaction on our part would indicate that we had fallen into a mental trap not in keeping with our responsibilities."

Illinois Commerce Commission v. Natural Gas Pipeline Company of America, 2 F.P.C. 218 (1940), affirmed 315 U.S. 575 after reversal on other grounds in 120 F. 2d 625 (C.A. 7).

In *Panhandle Eastern Pipeline Company v. Federal Power Commission*, 236 F. 2d 606 (C.A. 3), the Court rejected the company's claim that no reduction of a rate increase could be ordered until all phases of the case had been resolved. The Court held that the company had been given the opportunity to offer all of its

evidence in support of the severable elements of its claim, and had, in the view of the Commission, failed to make a prima facie showing in support thereof. Therefore, the Commission was under no obligation to postpone its disallowance of the items providing a rate reduction of about \$5 million annually.

In *State Corporation Commission of Kansas v. Federal Power Commission*, 206 F. 2d 690, 715-716 (C.A. 8) cert. denied 346 U.S. 922, the Court affirmed an interim reduction of approximately \$7½ million in increased rates filed by Northern Natural Gas Company, comprising elements as to which the Commission was of the view that the company had not made out a case.

In both the *Panhandle* and *State Corporation Commission* cases, *supra*, there remained other issues, including allocation matters to be disposed of by the Commission, but the rationale of these holdings is that the natural gas companies cannot continue to rely, and collect rates predicated, upon elements in the cost of service which have been found by the Commission to be overstated and unjustified.

Therefore, in the circumstances surrounding the instant case, the Commission not only had the authority but also the duty to issue an interim rate reduction when Tennessee's requested 7% rate of return was disallowed and the Commission determined that a 6½% rate of return (which was upheld in the Court below) was proper. Had the Commission remained inactive under these circumstances, the primary purpose of the Natural Gas Act to protect the ultimate consumer would have been thwarted. At the time the Commission determined that a 7% rate of return was excessive, and that not more than 6½% could be justified, it was obvious that many other complex issues in this case

could not be disposed of until many months later, and that therefore the consumers would have to continue to pay rates based on excessive claims if a rate reduction must await a determination of all the issues by the Commission in this rate proceeding. The difference between the 7% rate of return disallowed by the Commission and the 6 1/8%, which the Commission determined to be proper is approximately \$11 million. The Commission, therefore, properly issued the interim reduction order to afford immediate relief to consumers by reducing Tennessee's rates to effect the savings to consumers which this reduction of a substantial sum in the company's rates would effectuate. A reduction order at the conclusion of these lengthy proceedings prescribing just and reasonable rates for Tennessee could not, through refunds, make consumers whole for the unlawful part of the rates thus ended. As has been demonstrated, the Commission has the power and the duty to afford this protection to the consumer by providing immediate relief against excessive rates. The Commission has previously issued interim orders in situations similar to the instant case; and the interim order procedure has been upheld by the courts.

III. The Fifth Circuit Erroneously Limited the Commission's Rate Powers

The Fifth Circuit took a narrow and an erroneous view of the Commission's rate powers when it concluded that the Commission abused its discretion by issuing an interim order reducing the claimed rate of return by the amount it is unlawful before deciding the allocation issue. The view of the majority of the Court fails to give appropriate consideration to the initial rate making capacity of the interstate pipeline com-

pany and the burden of proof which is on the company to justify to the Commission the justness and reasonableness of the increased rate (Section 4(e)). Tennessee, in keeping with the statutory scheme of the Act, put together the various components constituting a cost of service upon which it based its increased rates, put the rates into effect, and then presented its evidence of justification in the hearing before the Commission.

The Commission did not question the other elements of Tennessee's cost of service as presented by Tennessee, including the zone allocations devised by Tennessee, and considered only the rate of return component which was ultimately determined at 6 1/8%. The pipeline company cannot complain if all of its presentation continues to be given effect in rates except the one element which the company could not justify and which was properly revised downward. The majority of the Court below was of the view that the existence of pending, unresolved issues affecting the determination of just and reasonable rates would cause Tennessee irreparable injury if the ultimate rates determined happened to be in excess of the rates set by the interim order. This is an erroneous view of the Commission's rate decision duties and powers.

A. A Pending Zone Allocation Issue Does Not Deprive The Commission's Use Of The Interim Order Procedure

The rate of return issue decided in this case is an outstanding example of a separable issue that can receive early and separate treatment in a rate case. On the other hand, the allocation issue discussed by the Court below, along with certain other issues, present problems of novelty requiring investigation which take

longer to develop, and which are of a nature that the Commission's consideration of them is enhanced by a hearing examiner's decision. The rate of return issue can be resolved with greater expedition than most of the other numerous and complex issues of a rate case. This is true because rate of return requires no extensive field investigation by the Commission staff, and it presents a repetitive broad judgment question with which the Commission is quite familiar without being materially aided by a hearing examiner's decision. The obstacle to separate determination of the rate of return issue as expressed in the opinion of two of the three Judges below is that a later determination of the allocation issue might affect the earnings in each of the six zones used by Tennessee. And that if the Commission approved an allocation formula different from that used by Tennessee, it was unreasonable to compel Tennessee to make a *pro tanto* correction of its rates before the allocation issue was decided. This speculation is without basis in reason or law when related up to the Commission's rate decision duties and powers under the Natural Gas Act.

The majority below, overlooked the fact that in deciding the reasonableness of one severable item of the cost of service, i. e., the proper rate of return, the regulatory agency does not guarantee the company that such a return will be earned, overall or by zones. On the contrary, the Commission merely decides that a rate of return is proper on the basis of a "test year," and that rates which will produce that return in the future are permissible, collectible and lawful rates. The end result in experience may be more or less than the estimates based on the "test year."

The fact that a zone allocation issue is still pending

does not in any manner restrict the Commission's authority to order an immediate rate reduction after it has determined that a pipeline company failed to justify its proposed rate of return and accordingly adjusted it downward to reflect its justness and reasonableness. The mere possibility that Tennessee might not be able to obtain all the revenues to which it would have been entitled had it made a proper filing, does not result from an interim rate reduction ordered by the Commission. Such a possibility could also occur without an interim rate reduction if it were determined at the conclusion of the entire case that Tennessee was entitled to more than the filed rates in some zones but required to make full refunds in other zones. Moreover, Tennessee should not complain that it has a greater risk now than if it had originally filed rates based on a proper and just return. In any event, the consumer should not be obligated to insure a natural gas company against the effects of discriminatory rates which the company itself prepares and files.

In the *State Corporation Commission* and the *Panhandle cases*, supra, pp. 21-22), interim orders were issued by the Commission while certain issues were still pending which, upon final determination, could have resulted in rates higher than the interim rates. In both of these cases, the same risks were involved to the companies filing new rates as Tennessee contends should preclude an interim order in the instant case. And the Courts there obviously considered this risk to belong to the pipeline company's stockholders rather than to the consumers.

Furthermore, it must be noted that zone allocation issues must be resolved in almost every natural gas rate increase case. If the majority opinion below was ap-

plied to all Commission proceedings respecting interim orders, it would mean that an interim order could never be issued where it was possible to raise questions concerning zone allocations in a later phase of a rate proceeding. The consumer would have to bear the burden of a pipeline company's excessive claims throughout an entire and lengthy rate proceeding. Clearly, this rationale would thwart the intent of Congress in enacting the Natural Gas Act.

B. The Fifth Circuit Erred In Concluding That The Allocation Issue Was Ripe For Decision

The majority opinion of the Court below erroneously concluded that at the time the Commission issued the interim rate reduction order it could have also decided the zone allocation issue. However, the fact is that the Commission was not in a position to decide the allocation issue when it issued the interim rate reduction order on August 9, 1960. The ultimate disposition of this allocation issue required an additional eighteen months after the Commission issued the interim order.¹³ Therefore, the allocation issue was not "ripe for decision" when the interim order was issued.

Under these circumstances, the Commission had good reason and exercised proper discretion when it decided the rate of return issue separately and adjusted the rates downward after its disposition without awaiting final determination of the allocation issue which required an additional year and one-half to decide. Certainly, there is no good reason to await the determination of all of the issues involved in Tennessee's cost of

¹³ Decided by the Commission on February 6, 1962, 42 P. U. R. 3rd 145.

service presentation and thus allow Tennessee to continue to collect its initially filed rates at the expense of the consumer merely because some issues cannot be decided as expeditiously as others. This is especially true when still other important issues involving Tennessee's cost of service remained unresolved at this time. Therefore, the majority opinion is erroneous in holding that the allocation issue was "ripe for decision."

IV: Refunds Are Not An Adequate Substitute for the Interim Order Procedure in Protecting the Consumer

In the broadest sense, the effect of the majority opinion of the Court below frustrates the primary objective of the Natural Gas Act which is to protect the ultimate consumer from exploitation at the hands of private pipeline companies. For the decision below appears to be based on the erroneous assumption that the consumers who continue to pay excessive rates are amply protected by the obligation of the pipeline company to refund excess charges found by the Commission to be unjust and unreasonable. The fact is that refund provisions are a poor substitute for an immediate reduction. The immediate reduction is a complete remedy. The refund is only a partial remedy.

The Natural Gas Act does not provide complete protection for the consumer who bears the burden of excessive rates, since, for the ordinary householder, the overpayment and refund process is not commensurate with an immediate rate reduction. Consumer residents are ambulatory, and in the years between the excess collection and the usual refund, the consumer population for given areas invariably shifts. Hence, the administering of a refund at the consumer level is therefore not only something in the nature of an approximation, but

also involves administrative detail and expense which comes out of and reduces the refund. Moreover, even in the event the ordinary householder does not change his residence, he cannot expect that the possibility of receiving a refund in the future will offset an immediate rise in his cost-of-living from the rate increase. The rate payer and not the pipeline pays all the costs of collecting and refunding the excess rates. He can never be made whole under that process. Only an immediate reduction of an unlawful rate can fully protect a consumer. There is nothing in the provisions of the Natural Gas Act which shift the risks of the pipeline business from the pipeline stockholders to the pockets of the consumers.

Another important factor is the 30 day notice and the rate suspension provisions of the Act. These provisions clearly demonstrate the Congress' awareness of the incomplete protection for the consumer of the refund provision of the Act. If Congress thought that the refund provision afforded the ultimate consumer adequate protection, there would have been no point in providing in the Act that the natural gas company in filing a new rate must await a thirty-day notice period before the new rate can go into effect. Also the new rate only goes into effect if the Commission does not suspend it for an additional five month period.

Conclusion

For these and the foregoing reasons, the judgment of the Court of Appeals should be reversed.

Respectfully submitted,

DAVID W. CRAIG,
*City Solicitor,
City of Pittsburgh,
Pennsylvania.*

CHARLES S. RHYNE,
EDWARD D. MEANS, Jr.
*Rhyme & Rhyme,
400 Hill Building,
Washington 6, D. C.
Attorneys for Petitioner, City of
Pittsburgh, Pennsylvania.*

August 1962.

(3620-2)

SEP 20 1962

IN THE

Supreme Court of the United States

JOHN F. DAVIS, CLERK

October Term, 1962

No. 48

FEDERAL POWER COMMISSION

Petitioner

TENNESSEE GAS TRANSMISSION COMPANY, THE
MANUFACTURERS LIGHT AND HEAT COMPANY,
THE OHIO FUEL GAS COMPANY AND UNITED
FUEL GAS COMPANY.

Respondents

No. 50

CITY OF PITTSBURGH

Petitioner

TENNESSEE GAS TRANSMISSION COMPANY, THE
MANUFACTURERS LIGHT AND HEAT COMPANY,
THE OHIO FUEL GAS COMPANY AND UNITED
FUEL GAS COMPANY.

Respondents

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF
APPEALS FOR THE FIFTH CIRCUIT

**BRIEF FOR RESPONDENTS, THE MANUFACTURERS
LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS
COMPANY AND UNITED FUEL GAS COMPANY**

BROOKS E. SMITH
ALFRED A. GREEN
120 East 41st Street
New York 17, New York

Counsel for
The Manufacturers Light and Heat
Company, The Ohio Fuel Gas
Company and United Fuel Gas
Company

R. K. TALBOTT
HERBERT W. BRYAN
1700 MacCorkle Avenue, S. E.
Charleston 25, West Virginia

Counsel for
United Fuel Gas Company

WILLIAM ANDERSON
EDWARD B. CALLAND
800 Union Trust Building
Pittsburgh 19, Pennsylvania

Counsel for
The Manufacturers Light and
Heat Company

W. F. LAIRD
RALPH N. MALLAFFEY
99 North Front Street
Columbus 15, Ohio

Counsel for
The Ohio Fuel Gas Company

Dated: September 19, 1962

INDEX

	PAGE
Table of Citations	ii
Definition of Terms	iv
Question Presented	1
Statutes Involved	3
Statement	3
Summary of Argument	8
Argument	13
I. In A Rate Proceeding Under the Natural Gas Act The Commission Has No Power To Reduce Tennessee's Zonal Rates Without Granting Parties A Hearing And The Decisional Process On The Essential And Controverted Issues of Cost Allocation and Rate Design	13
A. Sections 4 and 5 of the Natural Gas Act are Controlling	14
B. Section 16 of the Natural Gas Act Does Not Expand The Commission's Specific Statutory Powers	18
C. Petitioners' Judicial Precedents Are Inapposite	19
D. The Commission's Actions Violated Provisions of The Administrative Procedure Act	23
E. The Commission's Interim Order was an abuse of the administrative process	24
II. Arguments Advanced by Petitioners In An Effort To Support The Commission's Action Are Shown To Be Unsound	27
A. "Inadequacy of the Refund Provision"	28

	PAGE
B. Either Columbia Companies Or Tennessee or Both Are Prejudiced By The Interim Rate Reduction Order	29
C. Interim Rate Orders May be Used in Cer- tain Situations, But Not in the Instant Case.....	34
Conclusion	36
Appendix A	1a

TABLE OF CITATIONS

Court	
<i>Antiarillo-Borger Express, Inc. v. U. S.</i> , 138 F. Supp. 411 (N. D. Tex. 1945)	24
<i>Cobbledick et al. v. U. S.</i> , 309 U. S. 323 (1940)	35
<i>Episcopal Theological Seminary v. FPC</i> , 269 F. 2d 228 (CA4C 1959); certiorari denied <i>sub nom. Penn</i> <i>American Petroleum Corp. v. FPC</i> , 361 U. S. 895	22
<i>FPC v. Natural Gas Pipeline Co. of America</i> , 315 U. S. 575 (1942)	9, 16, 19, 20, 24
<i>Hope Natural Gas Co. v. FPC</i> , 134 F. 2d 278 (CA4 1943) (reversed on other grounds), 320 U. S. 591	19
<i>Hope Natural Gas Co. v. FPC</i> , 196 F. 2d 804 (CA4 1952), rehearing denied, 197 F. 2d 522	15
<i>Minneapolis Gas Co. v. FPC</i> , 294 F. 2d 212, 215 (CA4C 1961)	26
<i>Mississippi River Fuel Corp. v. Federal Power Com- mission</i> , 121 F. 2d 159 (CA8 1941)	22
<i>Mississippi River Fuel Corp. v. FPC</i> , 202 F. 2d 899 (CA3 1953)	14

<i>New England Divisions Case</i> , 261 U. S. 184 (1923) . . .	22
<i>Panhandle Eastern Pipe Line Co. v. Federal Power Commission</i> , 236 F. 2d 606 (CA3 1956)	19, 21
<i>State Corporation Commission of Kansas v. FPC.</i> 206 F. 2d 690 (CA8 1953), certiorari denied 346 U. S. 922	19, 21
<i>Tennessee Gas Transmission Co. v. FPC</i> , 283 F. 2d 729 (CA5 1960)	6
<i>Trunkline Gas Company v. FPC</i> , 247 F. 2d 159 (CA5 1957)	10, 24, 25
<i>West India Fruit & SS Co., Inc., et al. v. Seatrain Lines, Inc.</i> , 170 F. 2d 775 (CA2 1948)	24

Administrative

<i>Tennessee Gas Transmission Co., et al.</i> , Docket Nos. G-2352, et al., orders issued June 15, 1954, 13 FPC 623, and July 16, 1954, 13 FPC 631	5
<i>Tennessee Gas Transmission Co.</i> , Docket No. G-5259, orders issued October 6, 1955 and September 20, 1956 (unreported)	3
<i>Tennessee Gas Transmission Co.</i> , Docket No. G-11980, — FPC —, 42 PFC 3d 145 (February 6, 1962) pending on review <i>sub. nom. Manufacturers Light and Heat Co. v. FPC</i> , C. A. D. C. No. 17064	4, 21, 25, 33

DEFINITION OF TERMS

Columbia Companies—The Manufacturers Light and Heat Company, The Ohio Fuel Gas Company and United Fuel Gas Company.

Commission —Federal Power Commission.

Cost Allocation —An apportionment of the cost of service to the various rate zones and to the classes of service within each zone.

Cost of Service —Summary of all operating expenses and all other costs of providing service, including a reasonable return and income taxes associated with such return, for a specific twelve-months period.

"Floor" Rate —The last rate determined by the Commission to be "just and reasonable."

Lateful rates —Rates which the Commission has determined are *not* "unjust, unreasonable, unduly discriminatory, or preferential" so as to be final until modified prospectively under the Natural Gas Act.

"Legal" rates —Rates which have been put into effect subject to refund at the end of a suspension period to be continued during the refund period until superseded by *lateful* rates.

"Locked-in" Period —This period begins when rates filed under Section 4 of the Natural Gas Act become effective subject to refund and ends when rates subsequently filed become effective. Each succeeding and superseding change in rates is docketed by a separate

IN THE

Supreme Court of the United States

OCTOBER TERM, 1962

PLUMBER, DOWDY & ASSOCIATES,

Petitioner.

THE OHIO FUEL GAS COMPANY,

THE MANUFACTURERS LIGHT AND HEAT

COMPANY, THE OHIO FUEL GAS COMPANY,

AND UNITED FUEL GAS COMPANY,

Respondents.

AND THE DISTRICT OF COLUMBIA

Petitioner.

PLUMBER, DOWDY & ASSOCIATES, COMPANY,

THE OHIO FUEL GAS COMPANY, THE MANUFACTURERS

LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY

AND UNITED FUEL GAS COMPANY,

Respondents.

Nos. 48
and 50

BRIEF FOR RESPONDENTS, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY AND UNITED FUEL GAS COMPANY

Question Presented

Columbia Companies are substantial customers of Tennessee and are contending in this and several collateral proceedings still pending, that Tennessee is overcharging Columbia Companies and overcharging customers in other zones by the use of an improper method of cost allocation.

The Commission recognized that this controversy existed and set a prior collateral proceeding (Docket No. G-11980) to determine proper principles and methods of cost allocation which would be controlling. Before the decisional process was completed in said Docket No. G-11980, the Commission—in a separate (the underlying) proceeding, Docket No. G-19983—ordered Tennessee to reduce its rates solely because of a disallowance of a claimed rate of return of 7 per cent and a determination that the fair, just and reasonable rate of return for Tennessee is 6.8 per cent and *upon the basis of Tennessee's contested method of cost allocation*. Columbia Companies were precluded from presenting evidence in the rate of return phase of Docket No. G-19983 to show the allocation of such costs on Columbia Companies' method.

The question which arises under Sections 4 and 5 of the Natural Gas Act and Sections 5, 7, 8 and 12 of the Administrative Procedure Act is:

Did the Commission abuse its discretion or act outside the ambit of the statutes by ordering in Docket No. G-19983, the use of a contested method of cost allocation in requiring Tennessee to reduce its rates and make refunds (1) prior to a final determination in Docket No. G-11980 of the issue of proper principles and methods of cost allocation which issue is essential to a determination of (a) whether certain specific filed rates were unduly low and preferential and (b) whether the allowance of a finally determined fair rate of return to Tennessee would prevent overcharged customers from receiving refunds to which they were entitled, and (2) while precluding Columbia Companies from presenting evidence on cost allocation and rate design in the "rate of return" phase of Docket No. G-19983?

Statutes Involved

Sections 4 and 5 of the Natural Gas Act, 52 Stat. 821-833, as amended, 48 U.S.C. 717-717w, are set forth in the Commission's brief, pages 37-51. Pertinent Sections of the Administrative Procedure Act, 60 Stat. 237, 5 U.S.C. 1001-1011, are set forth in Appendix A, *infra*, page 1a of this report.

Statement

The Rate Controversy. The contested issue of the proper principles and methods of cost allocation among Tennessee's rate zones which forms the basis of Columbia Companies' contention to the Commission's use of the technique of cost allocation by "floor" order in the underlying administrative proceeding, although long before Tennessee made its rate filing on October 5, 1959, in Docket No. G-19983.

In 1955 the Commission officially recognized the existence of the disputed controversy in an order issued October 6, 1955, in Docket No. G-5259. Tennessee's "floor" rate proceeding, 150 F.2d 911, 30 AFTR 100, proceeding by order issued September 20, 1956, that the Commission refused to grant a Tennessee motion for "interim" rates, because all of the participants had not been given an opportunity to present evidence on the zoning issues and the Commission believed it would be premature, unfair and improper to do so.*

In 1957 the Commission set a specific administrative hearing, Docket No. G-11980, to determine a fair and equitable method of cost allocation for Tennessee so as to resolve the issue of whether Tennessee's rates were unduly preferential or prejudicial as among rate zones as contended by Columbia Companies and others (R. 622); Docket No.

*This order is quoted in full in Appendix B of the Commission's brief, pages 52-61, and was before the Court below (R. 642).

G-11980 was heard, the record was closed and briefs to the Examiner were filed four months prior to the date of issuance of the underlying administrative order now before the Court (R. 609). Subsequently, the Commission issued its order on principles and methods of cost allocation in Docket No. G-11980.* This order is pending before the Court of Appeals for the District of Columbia Circuit as Case No. 17064 on petition for review, filed by Columbia Companies.**

The G-19983 Hearing Before the Commission. At the hearing below in Docket No. G-19983, none of the intervenors, including Columbia Companies, were permitted the opportunity for the introduction of evidence on cost allocation. (R. 50-54, 291-295, 378-379). The Commission was fully informed of and acquiesced in the Examiner's refusal to permit such evidence (R. 577-583, 607-625).

The interim refund and rate reduction order was granted on oral motion of Staff Counsel (R. 525). Columbia Companies opposed the motion by verified pleading and on oral argument to the Commission although without objection to the final determination of a fair rate of return by interim order. Columbia's Memorandum pointed out to the Commission that there is an unresolved complaint by Columbia Companies that Tennessee has violated Section 4(b) of the Natural Gas Act with respect to undue rate discrimination (R. 612-613). It was also pointed out that this controversy has raged for many years and was evidenced by Tennessee's historical rate increases being *disproportion-*

**Tennessee Gas Transmission Company*, February 6, 1962, 42 PUR 3d 145.

**Also pending are two companion cases, Nos. 14897 and 15160, wherein Columbia Companies are seeking judicial review on the ground, among others, that the Commission erred in permitting Tennessee to misuse the underlying certificate proceedings for ulterior rate-making purposes to the injury of Columbia Companies.

ately higher in zones wherein Columbia Companies were served by Tennessee (R. 614).*

On July 19, 1960, Tennessee filed a motion to decide the rate of return issue in Docket No. G-19983, simultaneously with the cost allocation issue in Docket No. G-11980 while waiving the intermediate decision procedure in the latter case (R. 519-521). Columbia Companies opposed this motion primarily because the parties had literally spent years and hundreds of thousands of dollars on a voluminous and complicated record on the extremely important and seriously contested cost allocation issue and contended that the full decisional process, including the intermediate decision procedure, was essential (R. 658). Columbia Companies believed that the cost allocation issue was of paramount importance and, if the decision was expedited on that issue, it would expedite the determination of Tennessee's other rate cases (R. 659).

The Commission denied Columbia Companies' cross-motion on August 5, 1960, and commented that the present schedule of further hearings in Docket No. G-19983 appears to achieve the effect sought by the cross-motion (R. 523). However, Tennessee's rate cases are still unresolved by the Commission.**

*Columbia Companies have contended that this rate treatment was occasioned by reason of Tennessee's improvident expansion to New England and other new markets after 1950 at the expense of or subsidization by Columbia Companies. Tennessee expanded its service in its terminal Zones 1, 5 and 6 (including new markets in New York and New England) during the 1952-1958 period without substantial expansion of service to Columbia Companies. In 1954, an Examiner noted that Tennessee would earn only around 3% on its gas service in New England. See *Tennessee Gas Transmission Co. et al.*, Docket Nos. G-2352, et al., orders issued June 15, 1954, 13 FPC 623, and July 16, 1954, 13 FPC 631.

**By order issued August 31, 1962, the Commission has consolidated proceedings in Docket Nos. G-11980, G-17106 and G-19983 and scheduled a rehearing conference to consider *inter alia* "all matters remaining at issue in the above dockets" and a procedure for expediting the disposition of the "entire consolidated proceeding."

After the Commission issued its order of August 9, 1960, which required immediate interim refunds, Columbia Companies filed their petition for rehearing which, among other things, set out as specific error the Commission's statement that Tennessee and its customers would be put "in the same position" that they would have been in had Tennessee originally filed upon a 6 1/8 per cent instead of a 7 per cent rate of return basis (R. 582). Columbia Companies noted that under Section 7(c) of the Natural Gas Act the Commission was specifically deprived of the power to order Tennessee to *increase* its filed rates (R. 579) and, therefore, the fact that Tennessee had *voluntarily* filed for higher rates under Section 4(c) in other zones gave Columbia Companies an advantage in its zones which they would not have had had Tennessee originally filed upon a basis of 6 1/8 per cent return (R. 582-583). These matters were not commented upon by the Commission in its order denying applications for rehearing issued September 27, 1960 (R. 585-591).

Proceedings in the court below. Columbia Companies' petition for stay was denied by the Fifth Circuit, Judge Wisdom dissenting (R. 632-634; *Tennessee Gas Transmission Co. v. FPC*, 283 F.2d 729 (CA5 1960)). Tennessee complied with the order by making refunds and filing superseding rates which have been in effect since November 1, 1960.

* * On the merits, the Court Per Curiam order remanded the case to the Commission for further proceeding in view of the Court's disapproval of the Commission's action (1) in making its interim rate reduction order effective prior to a final determination of the allocation issue and (2) in ordering immediate refunds* (P. 644).

*It is Columbia Companies' position that the Commission's order is voidable and not void, so that on remand Tennessee could put its originally filed higher rates into effect *prospectively* only.

In addition, on the merits, Judge Wisdom *questioned* whether the Commission granted a "full hearing" contemplated in Section 4(c) of the Natural Gas Act; whether the order issued after a hearing in which the issue of allocation was heard was "lawful"; and whether the order made it so highly unlikely, it was unaffordable, Tennessee to earn a "just and reasonable return" as from the order lacking in weight and legal effect (R. 643), was *held*, however.

"that cost allocation among zones is an important element in determining whether the filed rates are excessive that it is unreasonable and an abuse of discretion to issue an interim rate order before deciding a pending allocation issue ripe for decision" (R. 643).

Judge Wisdom stated that

"The Commission's refusal to decide the allocation issue means that there is no basis for determining which of the filed rates in specific zones is unlawful, the extent to which individual rates should be reduced, or to which refunds are due. Moreover, the effect of the interim order is to compound the alleged discriminatory differential in favor of Zones 1, 5, and 6, although the Columbia companies, operating in Zones 2, 3, and 4, for several years have been endeavoring to have the Commission determine proper cost allocation among the zones." (R. 642)

Judge Tuttle dissenting, recognized that Columbia Companies were entitled under the statute as interested parties to a determination by the Commission of the complaint of undue preferences granted to the other zones in violation of Section 4(b) of the Natural Gas Act, but he believed that this determination should not necessarily be before the Commission can eliminate what it finds to be an unlawful increment in the price structure (R. 644).

Summary of Argument

I. The primary purpose of the Natural Gas Act is the protection of consumers. However, arbitrary rate reductions cannot be ordered for this salutary purpose, when customers of one zone are vying against customers of another zone without doing prejudicial harm to the ultimate consumers in one zone or another.

Columbia Companies have contested the rates in Tennessee's six zones as being unduly preferential and prejudicial in violation of Section 4(b) of the Natural Gas Act and have continually sought a determination as to allocation principles and methods which will result in their paying no more than their fair share of Tennessee's total cost of service. In these circumstances, Columbia Companies have a statutory right to a "full hearing" which includes the decisional process granted to them by Sections 4 and 5 of the Natural Gas Act and Sections 5(b), 7(c) and (d), 8(c) and 12 of the Administrative Procedure Act.

A. Sections 4(c) and 5(a) of the Natural Gas Act are controlling and they require a *full hearing and decision* before just and reasonable rates can be determined and refunds ordered of the portion of such rates found to be "not justified". The Commission's finding that the rates filed by Tennessee were "excessive" could not lawfully be made solely on the basis of the Commission's determination on the rate of return cost item since that determination was not made with respect to the particular rates of Tennessee, but with respect to a cost factor in Tennessee's aggregate cost of service. Although the Commission could generalize that Tennessee's rates filed on a 7% rate of return basis would yield excessive revenues, the Commission could not legally determine which of Tennessee's many rates were excessive (or too low) without properly allocating the reduced cost of service to zones and classes of customers. The factors of cost allocation and rate design are *inextricably intertwined*

with cost finding in determining those rates which meet the statutory standards of lawfulness. This is particularly true in this case where serious questions exist as to the discriminatory nature of Tennessee's separate individual zonal and customer rates *inter se*.

The diverse methods of allocation offered by the parties yield such drastically different results that even if there is a substantial reduction in Tennessee's total claimed cost of service, there may be no rate reductions in certain zones depending on the allocation method ultimately found lawful. This demonstrates that it is impossible for the Commission to find that the specific zone rates filed by Tennessee are unlawful until the cost allocation issue is determined.

B. Petitioners, apparently conceding the inconsistency of the Commission's action with the express dictates of Section 4, rely on Section 16 of the Natural Gas Act for statutory support for the Commission's action. Analysis of this section reveals it to be merely administrative in nature and thus offers no statutory basis for permitting the Commission to do that which is prohibited by Section 4, the section explicitly governing the regulation of rates.

C. Petitioners' reliance on earlier cases sanctioning the Commission's interim rate order procedure in certain circumstances is without merit. The crucial factor which dispositivey distinguishes those cases from the case at bar is that none of those cases involved a deferred cost allocation issue which could be applied retroactively to alter the results of the Commission's interim rate order and thereby prejudice the parties. On the contrary, these cases are authority for the proposition that parties must have "full opportunity to offer all their evidence both direct and in rebuttal, and full opportunity to cross-examine every witness". *FPC v. Natural Gas Pipeline Co. of America*, 315 U. S. 575 (583-584 (1942)). Columbia Companies did

not have this opportunity in the instant Docket No. G-19983 proceeding, and the controlling collateral case, Docket No. G-11980 is now pending in the Court of Appeals for the District of Columbia.

D. Although a proper determination of the issue of cost allocation was an indispensable prerequisite to a determination of the lawfulness of Tennessee's individual rates, the Commission permitted only Tennessee to put in evidence its own proposed system of cost allocation and did not allow Columbia Companies to develop an evidentiary record, either by its own evidence or by cross-examination of Tennessee's witnesses on basic issues such as cost allocation. The Commission's action was, therefore, in violation of Sections 5(b), 7(c) and (d), 8(b) and 12 of the Administrative Procedure Act.

E. The actions of the Commission herein are an abuse by it of the administrative process. In *Truykline Gas Company v. F. P. C.*, 247 F. 2d 159, (CA5 1957), the court declared that the Commission had no legal right to "change the rules in the middle of the game" and required the Commission to "adjudicate this matter within the full framework fashioned by it". In the instant case the Commission set Docket No. G-11980 as the proceeding in which to determine the basic issue of cost allocation which would be determinative of the propriety of rate reductions in Docket No. G-19983. By reducing rates in Docket No. G-19983 before Docket No. G-11980 is finally decided, the Commission has refused to decide the rate discrimination controversy within the framework that it itself fashioned.

In its order in Docket No. G-11980, issued *after* the complained of interim rate order, the Commission *did* modify Tennessee's method of cost allocation but not to the extent advocated by Columbia Companies who now have the matter on judicial review. The petition for review of

its earning an administratively determined rate of return, it is prejudiced to the extent that the *possibility* of earning the determined rate of return is eliminated by the improper action of the Commission itself.

By permitting Tennessee to file substitute rates based on a proper rate of return, but otherwise based on the company's own claims, Tennessee and its customers would *not* be placed in the same position as if Tennessee had originally filed increased rates predicated upon a proper rate of return. The Commission lacks the power to compel Tennessee to file higher rates involuntarily. Moreover, if the rates had not been suspended, they could be attacked only through a Section 5 proceeding which does not permit refunds. Under Section 4, where the rates were suspended and put into effect subject to refund, the action of the Commission does not leave the parties in the same position they would have been in if Tennessee originally filed rates based on a 6½ per cent rate of return, since that portion of the interim refund going to the already undercharged zones would have been available to Tennessee to make refunds to those properly entitled thereto.

C. In proper circumstances interim rate orders are legally permissible and may be in the public interest. There are numerous basic evils in piecemeal rate regulation which require that such regulation be strictly limited in application to those cases wherein its use is proper. Because of the particular fact situation in the instant case, particularly the danger of prejudice to the parties, the use of the interim rate order procedure is not proper.

ARGUMENT

1. In A Rate Proceeding Under The Natural Gas Act The Commission Has No Power To Reduce Tennessee's Zonal Rates Without Granting Parties A Hearing And The Decisional Process On The Essential And Controverted Issues of Cost Allocation And Rate Design.

Tennessee's rates for its six rate zones, presently or previously effective, and still subject to refund, are being contested as unduly preferential and prejudicial in violation of Section 4(b) of the Natural Gas Act by customers of Tennessee who are adversaries *inter se*. In addition, Tennessee and certain of its customers, including Columbia Companies, were and are litigants before the Commission and have conflicting interests. Tennessee is trying to get Commission approval for a number of different rate increases which varied as among zones and classes of customers within each zone. Columbia Companies, on the other hand, are seeking, among other things, a determination as to allocation procedures and methods which will result in them paying no more than their fair share of Tennessee's total cost of service.

As to Columbia Companies, the Court of Appeals said that:

the effect of the interim order is to continue the alleged discriminatory differential in favor of Zones 1, 5, and 6, although the Columbia companies, operating in Zones 2, 3, and 4, for several years have

been endeavoring to have the Commission determine a proper cost allocation among the zones." (R. 642) *

As intervening party litigants, Columbia Companies have a statutory right to a "full hearing" which includes the decisional process granted to them by the controlling statutes.**

Columbia Companies have certain inchoate rights with respect to payments they make to Tennessee in excess of their fair responsibilities. All of Tennessee's customers pay "legal" rates. To enforce the reason for the contingency of "legal" rates and the necessity for corporate security in the statutory scheme is "to safeguard customers" of Tennessee in their payments under the tariff pending the outcome of a hearing. *Mississippi River Fuel Corp. v. FPC*, 202 F. 2d 899, 903 (CA3 1953).

A. Sections 4 and 5 of the Natural Gas Act are Controlling

Section 4(c) of the Natural Gas Act describes the procedure to be followed when superseding rates are filed with

For example, the mathematical effect of the Commission's interim rate order was to reduce the companies' of Tennessee's originally filed rates as follows:

RATE REDUCTIONS

Rate Schedule	Southern Zone 1	Central Zone 2	Eastern Zone 3	Northern Zone 4	New York Zone 5	New England Zone 6
CD and C						
Demand	20.0c	25.0c	43.0c	45.0c	55.0c	60.0c
Commodity						
GS—Commodity	15c	21.5c	29c	32c	35c	43c
R and E						
Commodity	7c	11c	13c	14c	16c	21c
SS—Commodity			9c	11c	12c	
SS—Demand					60.0c	
T—Demand			40c	45c	45.0c	
Commodity				35c	36c	

**The statutes involved are Sections 4 and 5 of the Natural Gas Act and Sections 5(c), 7(c), and (d), 8(c), and 12 of the Administrative Procedure Act.

the Commission. It provides that the Commission shall have authority "to enter upon a hearing concerning the lawfulness of such rate, *and after full hearings, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective.*" (Emphasis supplied). This has been construed judicially to mean that the Commission "can make only such orders with respect thereto as would be proper" in a proceeding under Section 5(c) of the Natural Gas Act. *The People's Natural Gas Co. v. F. P. C.*, 196 F. 2d 804, 805 (CA4 1952), rehearing denied, 197 F. 2d 522.

Section 5(b) of the Act provides that: "Whenever the Commission, *after a hearing . . . shall find that any rate . . . is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate.*" (Emphasis supplied).

Section 4(c) provides further that the Commission shall have authority, "*upon completion of the hearing and decision, to order such natural gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified.*" (Emphasis supplied).

Thus, a *full hearing and decision* are required before just and reasonable rates can be determined and refunds ordered of the portion of such rates found to be not justified. In view of what has heretofore transpired it must be stressed that it is just and reasonable rates which must be determined after full hearing and before refunds can be ordered. In the instant case the Commission found that the rates filed by Tennessee were "excessive" (R. 532). It is submitted that such a finding could not lawfully be made solely on the basis of the Commission's determination on the rate of return lost item since that determination was made not with respect to the particular

rates of Tennessee, but with respect to a *cost* factor in Tennessee's aggregate cost of service. The essence of the problem is that although the Commission could generalize that Tennessee's rates filed on a 7% rate of return basis would yield excessive revenues, the Commission could not legally determine which of Tennessee's many rates were excessive (or too low) without first properly determining allocations of the reduced cost of service to zones and classes of customers. The cost allocation and rate design steps in the rate making process are equally as important as the cost determination steps. All are used to determine the various portions of cost which each customer should bear in rate charges.* These factors are inextricably interwoven in determining those rates which meet the statutory standards of lawfulness. This is particularly true in this case, where serious questions exist as to the discriminatory nature of the various rates *inter se*. Here, the Commission's error was to order Tennessee to use a contested method of cost allocation. Thus, the Commission required the assumption of an essential fact in issue to the prejudice of Columbia Companies.

If the cost allocation issue was one on which there was no basic disagreement among the parties, it might well be lawful for the Commission to have issued an interim order. Columbia Companies do not argue that this procedure is unlawful *per se*. In this case, however, the allocation issue is essential and is of such importance, that the Commission's failure to "decide" it prior to setting rates and

*In *FPC v. Natural Gas Pipeline Co. of America*, 315 U.S. 575, 584, 62 S. Ct. 736, 742, (1942) the Court stated:

"The establishment of a rate for a regulated industry often involves two steps of different character. . . . the second [step] is the adjustment of a rate schedule conforming to that level so as to eliminate discriminations and unfairness from its details." (emphasis added)

ordering refunds is contrary to the requirements of Section 4.

It must be borne in mind that a single rate is not involved. Tennessee filed separate individual rates for different zones and classes of customers. The unlawful level of each of these rates and their relationship to each other is in issue. The Commission's finding necessarily contemplates only that the filed rates are in totality excessive and does not consider the extent, if any, to which each individual rate is unlawful. This we submit contravenes the express requirements of Section 4(e).

Diverse methods of allocation were offered by the parties in the 1980 proceeding, the proceeding which, when finally resolved, will for the first time determine the proper method of allocating Tennessee's cost of service among the various rate zones for the purpose of designing rates. These methods yield such drastically different results that even if there is a substantial reduction in the total cost of service claimed by Tennessee, *there may be no rate reductions in certain zones depending on the allocation method ultimately found lawful* (R. 594-595, 598). This demonstrates that it is impossible for the Commission to find, as required by the act, that the specific zone rates filed by Tennessee are unlawful *until the allocation issue is determined*. As previously pointed out, the Commission had determined only that there should be an approximately \$11,000,000 *over-all* reduction in the aggregate revenue level due to the reduced rate of return. However due to the Commission's failure to decide the allocation issue prior to issuance of its order, it has no basis for determining which of the filed rates in the six zones are unlawful, the extent, if any, that the individual filed rates should be reduced and consequently to whom refunds were lawfully due. The Natural Gas Act is for the protection of *all* consumers and not just for those consumers given unduly preferential rate

treatment by virtue of Tennessee's contested cost allocation method.

B. Section 16 of the Natural Gas Act Does Not Expand The Commission's Specific Statutory Powers

It would appear that Petitioners concede the inconsistency of the Commission's action with the express provisions of Section 4 when they seek to find statutory authorization for the interim order in Section 16 of the Natural Gas Act.

Section 16 which is entitled, "Administrative powers of Commission; rules, regulations and orders" provides:

"Sec. 16. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and re-cind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this Act. *Among other things, such rules and regulations may define accounting, technical, and trade terms used in this Act; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission; the information which they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours.* (Italics supplied)

The crucial factor which dispositively distinguishes those cases from the case at bar is that none of those cases involved a deferred cost allocation issue which could be applied retroactively to alter the results of the Commission's interim rate order.*

The *Natural Gas Pipeline Co.* case, *supra*, related to a rate investigation by the Commission under Section 5(a) of the Natural Gas Act. The reduction of the company's rates to reflect the Commission's finding of a lower rate of return was final and could not be altered on a retroactive basis, since the Commission's power under Section 5 of the Act is restricted to orders having prospective effect only. Thus, a subsequent determination by the Commission of another issue could not operate to vary the result of the interim order.

In that case this Court was not asked to pass upon the propriety of the interim order procedure; rather, certain parties merely contended that "the order is invalid because the Commission did not itself fix reasonable rates as required by the act but instead merely directed the companies to file a new rate schedule which would result in the prescribed reduction in operating revenues." 351 U. S. at 583. Since the appropriateness of the interim order procedure was not questioned under the factual circumstance of that case, as was done in the instant proceeding, there clearly can be no conflict of decision.

Also of importance is the fact that the *Natural Gas Pipeline Co.* case did not even touch upon the problems of cost allocation among rate zones and rate design. Thus, that case did not involve the important issues that were before the Commission below and reviewed by the Fifth Circuit. Moreover, not only is the *Natural Gas Pipeline*

*This point was conceded by counsel for the Commission in the oral argument on October 19, 1960 before the Court below on the motion for stay. (R. 628)

Co. case clearly distinguishable on this ground, but also it is authority for the proposition that parties must have full opportunity to offer all their evidence both direct and in rebuttal, and full opportunity to cross-examine every witness. . . . (317 U.S. 583-584). Columbia Companies did *not* have this opportunity in the instant Docket No. G-11983 proceeding, and the controlling collateral case, Docket No. G-11980 is now pending before the Court of Appeals for the District of Columbia.

The *Panhandle* case, *supra*, likewise did not involve a deferred cost allocation issue which could be applied retroactively to disturb the Commission's interim order. To the contrary, it appears from the Court's decision that the problem of zone allocation had already been decided prior to the issuance of the interim order. (236 F. 2d at 611)

The issue in the *Panhandle* case was completely unrelated to the problem involved in the instant proceeding. Panhandle's objection before the Third Circuit did not relate to the effect of some deferred issue upon the interim order. The company merely asserted that the order was invalid since it prevented the parties from making a supplementary showing as to recent developments and changes in circumstances occurring during the pendency of the total rate proceeding. (236 F. 2d at 608)

State Corporation Commission of Kansas v. Federal Power Commission, supra, involved a natural gas system which was not even zoned at the time the Commission issued the interim order under review. Certain parties to the proceedings had presented evidence proposing zone rates. The Commission declined to decide the question due to the inadequacy of the evidence and designated a subsequent case, Docket No. G-1881, as being appropriate for the exploration of the problem of zone rates. (206 F. 2d at 712)

Since the Commission determined that the problem of zone rates should be decided in a separate *future* proceed-

ing, it is clear that its interim order could not be affected thereby and could be considered final as to the issues decided.

Moreover, an examination of the opinion by the Eighth Circuit indicates that no objection was raised as to the propriety of the interim order procedure as such under the facts of that case. The company involved, Northern Natural Gas Company, apparently made no showing as to any possible harm that could flow to it, retroactively or otherwise, as a result of the interim order, judging from the court's statement that "We are not shown any particular in which Northern was prejudiced by the Commission's action. . . ." (206 F. 2d at 716).

The other cases* cited by Petitioners as authority for the Commission's action are not in point. In the *New England Divisions Case*, the Court held that although the order issued by the Interstate Commerce Commission was provisional, nevertheless there had been a decision based on a full hearing on all the issues involved (261 U. S. at 200). The *Mississippi River Fuel Corp.* and *Episcopal Theological Seminary* cases do not bear on the issue of the lawfulness of the type of interim rate order here involved where cost allocation methods are yet to be finally determined. The purported relevance of these cases is not understood by Respondent.

Clearly, the facts and issues in the present case are quite different from those which existed in the decisions relied upon by Petitioners and those cases offer no authority for the action taken by the Commission in this case.

**New England Divisions Case*, 261 U. S. 184 (1923); *Mississippi River Fuel Corp. v. Federal Power Commission*, 121 F. 2d 156 (CA-8, 1941); *Episcopal Theological Seminary v. F. P. C.*, 200 F. 2d 228 (CA-DC, 1956); certiorari denied, *sub nom. Pan American Petroleum Corp. v. F. P. C.*, 361 U. S. 895.

D. The Commission's Actions Violated Provisions of The Administrative Procedure Act

The Administrative Procedure Act, 5 U.S.C. 1001-1011, gives "all interested parties" to Federal administrative proceedings "rights":

(a) to a "hearing, and decision upon notice and in conformity with sections 7 and 8" (Section 504, 5 USC 1001(b));

(b) to present their "case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts" (Section 706, 5 USC 1006(c)), so that such record shall be "the exclusive record for decision in accordance with section 8" (Section 704, 5 USC 1006(d));

(c) to a "ruling upon each such finding, conclusion, or exception presented" "as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the record," (Section 804, 5 USC 1007(b)), and

(d) to treatment whereby "all requirements or privileges relative to evidence or procedure shall apply equally to agencies and persons" (Section 12, 5 USC 1011).

It is submitted that by its interim order the Commission has denied all of these rights to Columbia Companies. In the underlying administrative proceeding Columbia Companies were not allowed to develop an evidentiary record, either by its own evidence or by cross-examination of Tennessee's witnesses, on the basic issue of cost allocation which is prerequisite to a determination of whether rate reductions for particular customers are proper. Cf.

Amarillo Border Express, Inc. v. U. S., (1945 U. S. Dist. Ct. ND Tex.) 138 F. Supp. 411; *FPC v. Natural Gas Pipeline Co. of America*, 315 U. S. 575, 583-584 (1942), 62 S.Ct. 736, 742; *West India Fruit & SS Co., Inc., et al. v. Seatrain Lines, Inc.*, 170 F. 2d 775 (CA2 1948).

It is submitted that the Commission acted as if the basic and material issues underlying the rate-discrimination controversy did not exist when it issued its interim piecemeal rate reductions on an incomplete record.

Although the Commission permitted one party, Tennessee, to put in its own style of cost allocation, it did not permit the others to do so. This is in direct violation of the mutuality of administrative due process expressed by Congress in Section 12 of the Administrative Procedure Act, 5 USC 1011.

E. The Commission's Interim Order was an abuse of the administrative process

The essence of the Commission's abuse of the administrative process is its indulgence in sheer expediency in the disposition of separate, but necessarily related, administrative proceedings so that a complicated basic controversy is arbitrarily decided for an interim period to the prejudice of Columbia Companies. This abuse strikes at the very heart of the administrative process and the ideal of administrative justice to all litigants under the Natural Gas Act and the Administrative Procedure Act.

A leading case on "abuse of administrative process" was decided by the Fifth Circuit in *Trunkline Gas Company v. FPC*, 247 F2d 159 (CA5 1957). In that case the Commission had ordered a full hearing into a phase of a natural gas company's rate and subsequently attempted to retrospectively limit the issues after the Examiner had issued his decision favorable to the company. The Court held that any such action is an abuse of the administrative process which the Commission may not do.

The Court said:

"Since we hold that the parties have not had the full and adequate hearing and determinations by the Commission in the merits of this matter as the statute requires, it would not be appropriate here for us to bypass the Commission, as it itself did . . . (page 163)

The Court declared that the Commission had no legal right to "change the rules in the middle of the game" and required the Commission to "adjudicate this matter within the full framework fashioned by it." (page 164)

In the present case the Commission's action is even more abusive to the administrative process than it was in the *Trinkline* case, *supra*. The Commission set Docket No. G-11980 as the proceeding in which to determine for Tennessee the basic and material issue of the principles and methods of cost allocation for rate making purposes which would be determinative of the propriety of rate reductions (if any) in Docket No. G-19983. The parties and the Examiner proceeded on that basis. Thus, by reducing rates in Docket No. G-19983 before Docket No. G-11980 is finally decided, the Commission refused to decide the rate discrimination controversy within the full framework fashioned by it. In its order in Docket No. G-11980 the Commission modified the Tennessee method of cost allocation somewhat, but not to the extent advocated by Columbia Companies who have brought the case before the Court of Appeals for the District of Columbia Circuit where it is pending as Case No. 17064. Columbia Companies submit that their petition for review of the Commission's cost allocation order in Docket No. G-11980 would be prejudiced if the Court does not uphold the Fifth Circuit in the matters now before it. Obviously, the rights of the parties to a fair hearing and judicial review have substance or else the whole administrative process becomes a sham

for Commission fiat and Section 19 of the Natural Gas Act becomes inapplicable:

Columbia Companies submit that the intent of Congress that Section 19 rate matters are to be given preference and are to be heard as speedily as possible, does not lessen the force of its declared intent that the Commission shall have a hearing and decision of such questions; and decide the state within the statutory scheme of the Natural Gas Act.

In short, in the administrative process speed cannot be its own excuse. If the administrative tribunal is faced with a difficult or complex problem which is essential to rate making and is contested, speed must give way to the demands of the decisional process.

In the instant case, the Commission issued its interim rate reduction order in spite of a long-unresolved rate discrimination controversy and at a time when the basic cost allocation issue was pending before its examiner—at its direction—awaiting a decision after the record was closed and four months after the last briefs were filed with said Examiner. The Commission's choice to act arbitrarily in this unique context on an incomplete record and outside the decisional framework was an abuse of discretion. Likewise, its failure to act first and promptly in Docket No. G-11960 is no excuse for its summary actions in Docket No. G-19983.

The courts have steadfastly refused to permit the Commission to act outside the scope of the Act it administers. Columbia Companies submit that the statutory framework is designed to protect all elements of the rate-paying public, including customer companies with differing positions as well as the natural gas company which serves them.

For example, Judge Prettyman held in *Minneapolis Gas Company v. FPC, et al.*, 294 F.2d 212, (CA DC 1961), that there are certain "binding necessities of a decisional

process" under the Natural Gas Act, which once substantially entered upon by, should not be avoided or short-circuited by resorting to due diligence process. Judge Prettyman fully realized "the pressure of events which apparently caused the Commission to adopt the course it did adopt." He sympathized with the difficulty in which the Commission finds itself, but held that "the statute does not permit the course it here proposes to follow."

In the instant proceeding before the Commission, it failed to consider seriously the issue of undue rate discrimination which has existed among Tennessee's zones and classes of customers within each zone for many years.

The Fifth Circuit's action below deprives the Commission of the use of the interim order technique only in those rate cases wherein there is a *bona fide* unresolved dispute on issues essential to the setting of lawful rates. It does not deprive the Commission of this technique in the proper case, such as those cited by the Commission in support of its action.

Call it "abuse of discretion" as Judge Wisdom did, or "abuse of process" as Columbia Companies do, it is submitted that the fragmentation of issues, which only when considered *in toto* properly present a rate question for decision, defeats rather than serves the policy of expedition evinced in Section 1(c) of the Act. This is amply demonstrated by the succession of multiple court and commission proceedings which the Commission's actions have brought forth in this and collateral cases. The placing of the cart before the horse is hardly the way to achieve speed.

II. Arguments Advanced By Petitioners In An Effort To Support the Commission's Action Are Shown To Be Unsound.

Unable to find specific statutory authority or a decisional plausibility for the issuance of the Commission's interim rate order, Petitioners have sought to interject other argu-

ments to support the Commission's action. These arguments are hereinafter considered and shown to be without merit.

A. "Inadequacy of the Refund Provision"

Petitioners argue that the action taken by the Commission was justified because the refund provisions of the Natural Gas Act are inadequate to protect the consumer which is the primary purpose of the Act. For example, at page 28 of its brief, the City of Pittsburgh states:

"The Natural Gas Act does not provide complete protection for the consumer who bears the burden of excessive rates, since for the ordinary householder, the overpayment and refund process is not commensurate with an immediate rate reduction."

It is further alleged that Congress recognized the inadequacy of the refund provision by enacting the suspension provision of Section 4 which, Petitioners argue, was enacted for the protection of consumers.

These arguments do not support the validity of the Commission's action in this case. If the Natural Gas Act offers insufficient protection for consumers, which we deny, it is up to the Congress and not the Commission to amend the statute. The Commission can only operate within the statutory framework already established for it. Of course, an administrative agency may exercise broad authority within the statutory authority granted to it to effectuate the clear Congressional purpose, but this authority does not sanction action contrary to and beyond the express provisions of the statute. The action here taken by the Commission is, precisely that, an express abnegation of the statutorily prescribed procedure of Section 4(e).

Likewise, whether or not Congress recognized the inadequacy of the refund provision in its enactment of the suspension provision of Section 4(e) is irrelevant to and in fact, negates the propriety of the Commission's action

herein. If Congress did in fact recognize any inadequacy, it may be argued that such inadequacy has been eliminated by the enactment of the suspension provisions. Otherwise, why did Congress not enact further legislation designed to cope with any such inadequacy? If Congress intended that the Commission be given the right to act as it has in the instant case, why was not such intention clearly spelled out? It is submitted that no authority for what the Commission has done here is present in the Act.

Aside from the statutory authority to do so, Columbia Companies deny even that the action of the Commission serves to protect consumers. It must be borne in mind that Columbia Companies *themselves* here represent the interests of millions of their own direct and indirect customers. Columbia's attempt to eliminate discrimination from the rates of Tennessee will benefit its customers who in the final analysis bear the burdens of such discrimination in the form of excessive rates. It is surprising to find the Pennsylvania Commission and the City of Pittsburgh purporting to represent consumers of Columbia, taking a position contrary to that of Columbia Companies. The position urged by the Pennsylvania Petitioners may well result in refunds to consumers in other jurisdictions at the expense of Pennsylvania consumers.

B. Either Columbia Companies or Tennessee or Both Are Prejudiced By The Interim Rate Reduction Order.

For years the Commission has recognized that Columbia Companies were objecting to Tennessee's rates to certain zones (particularly New England) as being unduly pref-

*This position is not understood by Columbia Companies and, apparently, is subject to change. At the hearing, counsel for the City of Pittsburgh opposed any refund made on the allocation basis proposed by Tennessee (R. 379), yet the City of Pittsburgh opposes Columbia Companies' efforts to see that all consumers get their full due without expense to those not responsible for the overcharges.

erential—that is, too low—as a result of Tennessee's method of cost allocation. Obviously then, when the Commission reduced "legal" rates that were already in controversy as being too low, that reduction was prejudicial to Columbia Companies. At pages 25-26 of its Brief, the Commission readily admits that its interim rate reduction order might preclude Tennessee from recovering a 6½ per cent return on rate base for past collections. However, as to Columbia Companies and other customers in Zones 2, 3 and 4, the Commission merely characterizes as "implausible" their prejudice which results from reducing "legal" rates in Zones 1, 5 and 6 before any decisional determination of the cost allocation issues on the basis of evidence. In short, the Commission summarily and arbitrarily reduced rates which may yet be found to have been too low.

Of course, since no evidentiary hearing on cost allocation was permitted in the "rate of return" phase of the underlying proceeding, the extent of the possible prejudice to Columbia Companies cannot be shown precisely. However, the record does show by reference to Docket No. G-11980 that the originally filed G-11980 rates to New England (which were reduced by the interim order) failed to recover the costs which Columbia Companies' method of cost allocation would have occasioned by more than \$5,000,000 per year (R. 613**).

In answer to Columbia's claim of possible injury, Petitioners argue that in any event Columbia can recoup against Tennessee.

It is obvious that any recoupment from Tennessee would come from funds above and beyond those brought into issue by the Tennessee rate filing, assuming a 6½ per cent re-

*Commission Brief, page 41.

**The figure \$5,238,011 appears in two places on the schedule in the record. This was a typographical error and was corrected in oral argument before the Fifth Circuit. The figure opposite line 5 (New York) under column 4 should be \$1,065,500.

turn to Tennessee. In other words, any moneys thus re-
 ceived by Columbia Companies from Tennessee would re-
 sult in Tennessee not earning the 6 1/2 per cent return found
 by the Commission to be proper. It is argued, however,
 that "the Commission's determination that a 6 1/2 percent
 (as opposed to a 7 percent) rate of return is proper does
 not carry with it a guarantee that Tennessee must in all
 events be permitted to retain revenues affording that rate
 of return for the interim period." However, although
 regulation does not *guarantee* certain net revenues because
 of conditions beyond the control of those involved, never-
 theless a business shall not be denied the *possibility* of a
 return found to be just and reasonable *because of the im-
 proper action of the regulator itself*. Purportedly, the
 Commission has allowed Tennessee a rate of return of 6 1/2
 per cent. Tennessee should have a right to a *possibility* of
 recovering such a return at least during the interim period
 without having to count on prevailing ultimately in the cost
 allocation controversy. If Tennessee is permitted a return
 of 6 1/2 per cent, then it will be at the expense of Columbia
 Companies.

Thus, either Columbia Companies or Tennessee or both
 may be irreparably damaged by the Commission's action.

It is urged, however, and this *is* the core of Peti-
 tioners' argument, that by permitting Tennessee to file
 substitute rates based on a proper rate of return, but other-
 wise based on the company's own claims, Tennessee and
 its customers would be placed in the same position as if
 Tennessee had originally filed increased rates predicated
 upon a proper rate of return. This was alleged by the Com-
 mission in its interim rate order (R. 535-536). We submit
 that this reasoning is fallacious. If Tennessee's rates had
 been permitted to go into effect without suspension, they
 could be attacked only through a Section 5 proceeding.

*Brief for the Federal Power Commission, pages 45-46.

Since this section permits only *prospective* action with no reparations for past rates, there would be no issue with respect to refunds. However, under Section 4, where the rates were suspended and then put into effect subject to refund, the Commission's action in issuing the interim order does not leave the parties in the same position they would have been in if Tennessee originally filed rates based on a 6½ per cent rate of return. This is because that portion of the refund of \$11,000,000, which came from the under-charged zones, would have been available to Tennessee to make refunds. As the court below properly found:

"It is true, of course, that the allocation of costs in all six schedules was made by Tennessee; that if these allocations are correct and are approved Tennessee will not be damaged; that the burden rests on the applicant to justify each rate increase. But conditions change, costs are not static, and rates are at best an educated guess. It seems that in filing rates a public utility should not be held, at its peril, to the requirement of foretelling the decision of the Commission on the correctness of the rates. The statute appears to have been designed on the assumption filed schedules will have to be adjusted. Lawful rates may be determined only after a full hearing; until the Commission fixes rates the utility is protected by being allowed to collect at the filed rate but under bond [*] and subject to refund, and the consumer is protected by the refund of excess charges with 7 percent interest." (R. 643)

We submit that the definite possibility of injury directly due to the issuance of the interim rate order herein has been

[*] The undertaking prescribed by the Commission and filed by Tennessee was that Tennessee would "refund at such times and in such manner as may be required by final order of the Commission, the portion of the increased rates found by the Commission in this proceeding not justified, together with interest thereon at the rate of 7 percent per annum." (R. 507-508) (Emphasis supplied.)

demonstrated. In this respect, the instant case materially differs from other "interim order" cases which did not contain any apparent cost allocation or rate design issues.

At page 42, footnote 30, of its brief, The Commission likens Columbia Companies' interest to a "stakeholder". This raises a very pointed comparison which can be used to explain the exact status of Columbia Companies in this proceeding, and the nature of the Commission's end as to them.

A "stakeholder" is one who holds money which is claimed by rival claimants, but in which he himself claims no interest. In order to prevent himself from being prejudiced by proceedings instituted by the rival claimants, the stakeholder can file a bill of interpleader to make the rival claimants litigate among themselves rather than with the stakeholder.

Here, in an analogous way, Tennessee (not Columbia Companies) is the primary stakeholder and Columbia Companies are claimants for refunds for a portion of Tennessee charges which are "not justified".* However, it cannot be settled as to which rates and charges are or were "not justified", until the issue of cost allocation and complaints of undue rate discrimination are settled finally.**

It is obvious that a judge in an interpleader suit would not direct payment of a portion of the stake if he had not determined on the evidence that the party receiving it had a right to same, and, if so, the magnitude of that portion.

*However, there are limits to this analogy, because Tennessee may be more than a mere stakeholder depending on the results of other elements of fixing for it just, reasonable and non-discriminatory rates.

**As aforesaid, the cost allocation determination has been made in application of the Tennessee method and is pending before the Court of Appeals for the District of Columbia Circuit on petition for review filed by Columbia Companies in Case No. 17064.

Here, by its interim order, the Commission has arbitrarily and summarily decided, for example, that Tennessee's New England customers are entitled to a refund (part of the stake), although Columbia Companies have contended that not only should the New England customers have received no refunds at all, they should have paid more to Tennessee.

Tennessee cannot be sure, pending final Commission action, of how much of over-collections plus under-charges is due to each particular party. It may be that no refunds are due to the New England customers and that they actually should have paid more to Tennessee. By withdrawing some of the total receipts prior to a final determination, the Commission's action is akin to a court in an interpleader suit dividing up a portion of the stake prior to determining which of the claimants is entitled to what share of the total.

In the instant case, the action of the Commission results in withdrawing a portion of the money which may be due Columbia Companies and paying it out to other parties.

C. Interim Rate Orders May Be Used in Certain Situations, But Not in the Instant Case

Columbia Companies concede that in proper circumstances interim rate orders are legally permissible and may be in the public interest. Columbia Companies respectfully point out, however, that there are numerous basic evils in piecemeal rate regulation which require that such regulation be strictly limited in application to those cases where its use is proper. For example, in the underlying proceeding it is impossible to predict what effect subsequent modifications of the cost of service being litigated will have upon the costs to be allocated to various zones and classes of jurisdictional customers within each zone, as well as the classification of costs to the demand and commodity cost com-

ponents.* Furthermore, piecemeal rate regulation inherently causes delays in a final determination of rate controversies before the administrative body.

Moreover, if piecemeal rate orders are issued having elements of finality which are contested by certain of the parties, there will necessarily have to be piecemeal judicial review. The Law has always frowned upon the multiplicity of suits at the trial stage as well as at the appellate stage. Cf. *Cobbledick et al. v. U. S.*, 309 U. S. 323, 325, 60 S. Ct. 540, 541 (1940), where Justice Frankfurter said

"Congress from the very beginning has, by forbidding piecemeal disposition on appeal of what for practical purposes is a single controversy, set itself against enfeebling judicial administration. Thereby is avoided the obstruction to just claims that would come from permitting the harassment and cost of a succession of separate appeals from the various rulings to which a litigation may give rise, from its initiation to entry of judgment. To be effective, judicial administration must not be leaden-footed. Its momentum would be arrested by permitting separate reviews of the component elements in a unified cause."

Finally, piecemeal rate regulation must necessarily mean piecemeal refunds. At page 33, footnote 23, of its Brief, the Commission noted the "complexities" of refunds. It is because of these complexities that Columbia Companies submit that either refunding should be kept at the minimum and as the *last* step in the rate-making process as a result of the *final* determination of just and reasonable nondiscriminatory rates or else it should be confined

*For example, the cost per Mcf for gas in the field is recognized as a uniform commodity cost payable on a volume basis in all zones. The return on facilities as a cost is entirely different, depending upon the investment in facilities and types of service rendered by them in the various zones.

to settlements or special arrangements where the litigants are not prejudiced in their positions still to be determined pursuant to the administrative process.

CONCLUSION

For the foregoing reasons the judgment of the Court of Appeals for the Fifth Circuit should be affirmed.

Respectfully submitted,

BROOKS E. SMITH
120 East 41st Street
New York 17, New York

Counsel for
The Manufacturers Light and
Heat Company
The Ohio Fuel Gas Company
United Fuel Gas Company

Dated: September 20, 1962

APPENDIX A

THE ADMINISTRATIVE PROCEDURE ACT, 60 Stat. 237,
5 USC 1001 *et seq.* provides, in pertinent part, as follows:

* * *

SEC. 5. [5 U. S. C. § 1004]. In every case of adjudication required by statute to be determined on the record after opportunity for an agency hearing, except to the extent that there is involved (1) any matter subject to a subsequent trial of the law and the facts de novo in any court; (2) the selection or tenure of an officer or employee of the United States other than examiners appointed pursuant to section 11; (3) proceedings in which decisions rest solely on inspections, tests, or elections; (4) the conduct of military, naval, or foreign affairs functions; (5) cases in which an agency is acting as an agent for a court; and (6) the certification of employee representatives—

* * *

(b) *Procedure*.—The agency shall afford all interested parties opportunity for (1) the submission and consideration of facts, arguments, offers of settlement, or proposals of adjustment where time, the nature of the proceeding, and the public interest permit, and (2) to the extent that the parties are unable so to determine any controversy by consent, hearing, and decision upon notice and in conformity with sections 7 and 8.

* * *

SEC. 7. [5 U. S. C. § 1006]. In hearings which section 4 or 5 requires to be conducted pursuant to this section—

(c) *Evidence*. Except as statutes otherwise provide, the proponent of a rule or order shall have the burden of proof. Any oral or documentary evidence may be received; but every agency shall as a matter of policy provide for

the exclusion of irrelevant, immaterial, or unduly repetitious evidence and no sanction shall be imposed or rule or order be issued except upon consideration of the whole record or such portions thereof as may be cited by any party and as supported by and in accordance with the reliable, probative, and substantial evidence. Every party shall have the right to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts. In rule making or determining claims for money or benefits or applications for initial licenses any agency may, where the interest of any party will not be prejudiced thereby, adopt procedures for the submission of all or part of the evidence in written form.

(d) *Record*.—The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, shall constitute the exclusive record for decision in accordance with section 8 and, upon payment of lawfully prescribed costs, shall be made available to the parties. While any agency decision rests on official notice of a material fact not appearing in the evidence in the record, any party shall on timely request be afforded an opportunity to show the contrary.

SEC. 8. [5 U. S. C. § 1007]. In cases in which a hearing is required to be conducted in conformity with section 7—

* * *

(b) *Submittals and decisions*.—Prior to each recommended, initial, or tentative decision, or decision upon agency review of the decision of subordinate officers the parties shall be afforded a reasonable opportunity to submit for the consideration of the officers participating in such decisions (1) proposed findings and conclusions, or (2) exceptions to the decisions or recommended decisions

of subordinate officers or to tentative agency decisions, and (3) supporting reasons for such exceptions or proposed findings or conclusions. The record shall show the ruling upon each such finding, conclusion, or exception presented. All decisions (including initial, recommended, or tentative decisions) shall become a part of the record and include a statement of (1) findings and conclusions, as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the record; and (2) the appropriate rule, order, sanction, relief, or denial thereof.

* * *

SEC. 12. [5 U.S.C. § 1011]. Nothing in this Act shall be held to diminish the constitutional rights of any person or to limit or repeal additional requirements imposed by statute or otherwise recognized by law. Except as otherwise required by law, all requirements or privileges relating to evidence or procedure shall apply equally to agencies and persons. If any provision of this Act or the application thereof is held invalid, the remainder of this Act or other applications of such provision shall not be affected. Every agency is granted all authority necessary to comply with the requirements of this Act through the issuance of rules or otherwise. No subsequent legislation shall be held to supersede or modify the provisions of this Act except to the extent that such legislation shall do so expressly. This Act shall take effect three months after its approval except that sections 7 and 8 shall take effect six months after such approval; the requirement of the selection of examiners pursuant to section 11 shall not become effective until one year after such approval, and no procedural requirement shall be mandatory as to any agency proceeding initiated prior to the effective date of such requirement.

SUPREME COURT, U. S.

Office Supreme Court, U.S.

FILED

SEP 22 1962

JOHN F. DAVIS, CLERK

IN THE
Supreme Court of the United States

OCTOBER TERM, 1962

No. 48

FEDERAL POWER COMMISSION, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY and UNITED FUEL GAS COMPANY, *Respondents*.

No. 50

CITY OF PITTSBURGH, PENNSYLVANIA, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY and UNITED FUEL GAS COMPANY, *Respondents*.

On Writs of Certiorari to the United States Court of Appeals
for the Fifth Circuit

**BRIEF FOR RESPONDENT TENNESSEE GAS
TRANSMISSION COMPANY**

W. C. BRADEN, JR.
402 Solar Building
Washington 5, D. C.

HARRY S. LITTMAN
JACK WERNER
HAROLD L. TALISMAN
317 Wyatt Building
Washington 5, D. C.

*Attorneys for Tennessee
Gas Transmission Company*

INDEX

	Page
Opinions Below	1
Jurisdiction	2
Questions Presented	2
Statute Involved	2
Statement of the Case	2
Summary of Argument	8
Argument	12
I. The Interim Order Procedure as Applied in This Case Is Unlawful and Unfair	14
The Background of the Zone Allocation Issue	15
A. The Commission Cannot Set Aside Rates Until They Are Found Excessive	19
B. Section 16 of the Act Does Not Empower the Commission to do Acts Which Are Beyond Its Authority Under Other Sections of the Act	22
C. The Commission's Attempted Justification for the Interim Order Procedure as Applied Herein Is Without Merit	23
D. The Commission Had Lawful Alternatives Available for Carrying Out Its Objective ..	29
E. The Commission Has No Judicial Sanction for Applying the Interim Order Procedure in a Case Such as This	32
F. The Commission's Contentions With Regard to the Remoteness of Injury to Tennessee Are Without Merit	34
II. Affirmance of the Decision Below Would Bring a Proper and Just Result	36
Conclusion	37
Appendix A	38

CASES CITED

Page

<i>Atlantic Refining Co. v. Public Service Comm. of N. Y.</i> , 360 U.S. 378 (1959)	31
<i>Atlantic Seaboard Corp.</i> , 11 F.P.C. 43 (1952)	13
<i>American Louisiana Pipe Line Company</i> , F.P.C. Opin- ion 363	27
<i>Bluefield Waterworks and Improvement Co. v. Public Service Comm. of W. Va.</i> , 262 U.S. 679 (1923)	24
<i>Colorado Interstate Gas Co. v. F.P.C.</i> , 142 F.2d 943 (10 Cir., 1944)	21
<i>Colorado Interstate Gas Co. v. F.P.C.</i> , 324 U.S. 581 (1945)	25
<i>El Paso Natural Gas Co.</i> , Docket No. G-4769, order issued December 27, 1961	28
<i>F.P.C. v. Panhandle Eastern Pipe Line Co.</i> , 337 U.S. 498 (1949)	22
<i>F.P.C. v. Natural Gas Pipeline Co.</i> , 315 U.S. 575 (1942)	32
<i>F.P.C. v. Sierra Pacific Power Co.</i> , 350 U.S. 348 (1956)	24
<i>Hope Natural Gas Co. v. F.P.C.</i> , 196 F.2d 803 (4 Cir., 1953)	20, 31
<i>Natural Gas Pipeline Co. v. F.P.C.</i> , 120 F.2d 625 (7 Cir., 1941)	32
<i>Northern Natural Gas Company</i> , 11 F.P.C. 278 (1952)	34
<i>Northern Natural Gas Company</i> , 11 F.P.C. 1327 (1952)	34
<i>Panhandle Eastern Pipe Line Co. v. F.P.C.</i> , 236 F.2d 606 (3 Cir., 1956)	32, 33, 34
<i>State Corporation Commission of Kansas v. F.P.C.</i> , 206 F.2d 690 (8 Cir., 1956)	32, 33
<i>Tennessee Gas Transmission Company</i> , Docket No. G- 5259, FPC order issued September 20, 1956	16, 17
<i>Tennessee Gas Transmission Company</i> , 18 F.P.C. 428 (1957)	3, 6
<i>Tennessee Gas Transmission Company</i> , Docket No. G- 19983, Examiner's Decision issued May 28, 1962 ..	3
<i>Tennessee Gas Transmission Company</i> , Docket No. G- 11980, FPC order issued April 30, 1959	5
<i>Tennessee Gas Transmission Company</i> , Docket No. G- 11980, Examiner's Decision issued February 13, 1961	14
<i>Tennessee Gas Transmission Company</i> , 42 P.U.R. 3d 145 (1962)	5, 15, 18, 26, 27, 36
<i>United Gas Pipe Line Co. v. Mobile Gas Service Corp.</i> , 350 U.S. 332 (1956)	9, 20, 21
<i>Willmut Gas and Oil Co. v. United Gas Pipe Line Co.</i> , 12 F.P.C. 432 (1953)	22

STATUTES AND REGULATIONS

	Page
Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821-823, as amended, 15 U.S.C. 717-717w:	
Section 4, 15 U.S.C. 717c	2, 19, 22, 23
Section 4(d), 15 U.S.C. 717c(d)	19
Section 4(e), 15 U.S.C. 717c(e)	8, 19, 20, 21, 23, 31, 33
Section 5, 15 U.S.C. 717d	22, 23
Section 5(a), 15 U.S.C. 717d(a)	20, 21, 22, 32
Section 16, 15 U.S.C. 717o	9, 23

MISCELLANEOUS

<i>American Gas Association, Gas Facts</i> , 1960	30
---	----

IN THE
Supreme Court of the United States

OCTOBER TERM, 1962

No. 48

FEDERAL POWER COMMISSION, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY and UNITED FUEL GAS COMPANY, *Respondents*.

No. 50

CITY OF PITTSBURGH, PENNSYLVANIA, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY and UNITED FUEL GAS COMPANY, *Respondents*.

On Writs of Certiorari to the United States Court of Appeals
for the Fifth Circuit

**BRIEF FOR RESPONDENT TENNESSEE GAS
TRANSMISSION COMPANY**

OPINIONS BELOW

The opinions of the Court of Appeals for the Fifth Circuit (R. 635-646) are reported at 293 F. 2d 761. The orders of the Federal Power Commission (R. 524-540, 587-591)¹ are reported at 24 F.P.C. 294 and 525.

¹ The record references "(R. 524-540)" are to the pages of the Joint Appendix.

JURISDICTION

The jurisdictional requisites are adequately set forth in the briefs for the petitioners.

QUESTIONS PRESENTED

(1) Does the Federal Power Commission have authority under Section 4 of the Natural Gas Act to set aside filed individual zone rates, and to order reductions in rates and refunds prior to a determination of the zone allocation issue which is an inseparable part of determining whether the filed individual zone rates are just and reasonable?

(2) Where the issue of zone allocation has been thoroughly tried and briefed and is awaiting decision, did the Commission abuse its discretion in failing to decide that issue prior to ordering an interim reduction in rates and refunds where such action could in fact deprive Tennessee Gas Transmission Company of earning the rate of return prescribed by the Commission's interim order?

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717-717w, are set out in Appendix A to the Brief for Petitioner in No. 48.

STATEMENT OF THE CASE

Tennessee Gas Transmission Company (Tennessee) owns and operates a natural gas pipeline system extending some 2,200 miles in a northeasterly direction from its sources of supply in Texas and Louisiana traversing sixteen states² and terminating in New England. The area in which Tennessee transports and

² Tennessee's pipeline system extends through Texas, Louisiana, Arkansas, Mississippi, Alabama, Tennessee, Kentucky, West Virginia, Ohio, Pennsylvania, New Jersey, New York, Massachusetts, New Hampshire, Rhode Island and Connecticut.

sells natural gas is divided into six rate zones for rate-making purposes, with rates differing among the zones to give effect to distance of transmission from source of gas supply and other factors.

Tennessee, on October 5, 1959, filed schedules of increased rates for each zone with the Federal Power Commission (R. 502-504). The major reason for such filing was to recover the increased cost to Tennessee of natural gas purchased from producers who had filed increased rates with the Commission (R. 503).³

Additionally, Tennessee's rates reflected increases in taxes, wages and the cost of debt capital incurred in financing expansions of pipeline capacity approved by the Commission (R. 503). Since the interest cost on long-term debt is considered by the Commission as an integral part of the over-all return allowance, Tennessee's rates reflected an increase in the rate of return on its investment to 7 percent solely to recover the increased cost of such debt. No increase in the return previously allowed by the Commission to common stockholders was requested.⁴

³ For example, investigation by the Commission's Staff revealed that Tennessee's actual cost of purchased gas was 18.23¢ per Mcf for the first six months immediately following the month in which Tennessee's rates became effective (April, 1960), as compared to a unit cost of 14.55¢ per Mcf for the 12 months ended July, 1959 (the test year). Based on the volume of gas purchased during the test year (688,354,803 Mcf) this represented an increase of approximately \$25,000,000 in the cost of purchased gas. *Tennessee Gas Transmission Company*, Docket No. G-19983, Examiner's Decision issued May 28, 1962, pages 3, 6-7 (unreported).

⁴ In Tennessee's last decided rate case, the Commission found that a 6% over-all return, which yielded a 13.71% return on Tennessee's common equity investment, was reasonable. *Tennessee Gas Transmission Company*, 18 F.P.C. 428, 430, 439, 441 (1957). In the case at bar, due to the increase in cost of debt, a 7% over-all return yielded a 13.08% return on Tennessee's common equity, as found by the Commission in the order under review (R. 530).

By order issued November 4, 1959, the Commission suspended the effective date of the increased rates and ordered a hearing to determine the "lawfulness" of the rates which had been filed (R. 502-505). Following a five-month period of suspension, the rates became effective April 5, 1960, subject to an undertaking by Tennessee, required by Commission order, to (R. 505-503):

*** refund at such times and in such manner as may be required by final order of the Commission, *the portion of the increased rates found by the Commission in this proceeding not justified, together with interest thereon at the rate of 7 percent per annum* ***⁵

Hearings commenced on February 2, 1960, and continued intermittently until recessed on May 25, 1960. At such hearings Tennessee presented its evidence on cost of service including evidence as to rate of return. The Commission Staff and one intervenor presented evidence limited solely to the question of rate of return. At the conclusion of this portion of the hearings, Commission Staff counsel moved that the hearing be divided into two phases, the first phase to deal solely with the issue of rate of return, and the remaining issues to be reserved for a later stage of the proceeding. Staff counsel further proposed that upon completion of the first phase of the proceeding, the Examiner's decision be omitted; that the Commission issue a decision determining the fair rate of return for Tennessee; and that the Commission issue an interim order requiring Tennessee to reduce its rates and make refunds, in the event the Commission should conclude that the fair

⁵ Unless otherwise indicated, emphasis is supplied throughout this brief.

rate of return is less than claimed by Tennessee (R. 377-378).

When Staff counsel made his motion, there was pending before the Commission in the instant proceeding, and in another pending rate proceeding involving Tennessee (Docket No. G-11980), the zone allocation issue, which, when resolved, would for the first time determine the method to be used in allocating Tennessee's cost of service among its six rates zones and various classes of services. Almost a year and one-half prior to the interim order in this case, the Commission had ruled that determination of the allocation issue should be expedited and, to that end, severed that issue for separate and prior hearing and determination in Docket G-11980.⁶ At the time Staff counsel made his motion, the allocation issue had already been tried and briefed and was awaiting decision by the Examiner. Additionally, the Examiner in the instant proceeding, who is also the Examiner in Docket G-11980, had ruled that the determination of the allocation issue in Docket G-11980 would govern the method of allocating Tennessee's cost of service in this case (R. 50-1).⁷

Since determination of the allocation issue is required in order to translate the cost of service into rates for the various zones and services, Tennessee opposed the Staff's motion for an interim order on the

⁶ *Tennessee Gas Transmission Company*, Docket G-11980, order issued April 30, 1959 (unreported).

⁷ The Commission subsequently held that the decision on zone allocation in Docket No. G-11980 would apply to the case at bar and future cases, *Tennessee Gas Transmission Company*, 42 PUR 3d 145, 150 (1962), pending on review, *sub nom. Manufacturers Light and Heat Co. v. F.P.C.*, CADC No. 17064.

ground, *inter alia*, that such order would be illegal unless the Commission simultaneously determined the allocation issue (R. 591-606). On July 19, 1960, Tennessee filed a motion with the Commission requesting it to determine the allocation issue simultaneously with the issue of rate of return (R. 519-521). By order issued August 5, 1960, the Commission denied Tennessee's motion (R. 521-523).⁸

On August 9, 1960, the Commission issued its interim order, here involved, adopting the Staff's proposed procedure. Although the Commission found that the evidence supported Tennessee's claimed increase in cost of debt (R. 529), it denied Tennessee the rate of return requested. Instead of increasing the over-all rate of return to compensate for this increase in cost of debt, the Commission reduced the return on common stock equity 26% below that previously allowed as reasonable⁹ and thereby arrived at a 6½% over-all return instead of the 7% over-all return requested by

⁸ Petitioner in No. 48 (Br. p. 5) alleges that the motion filed by Tennessee was untimely since it was not filed within five days after the close of hearings on the allocation issue, but fails to mention that it was not denied on that ground. Moreover, good cause to omit the intermediate decision on allocation did not arise until the Staff made its motion for an interim decision on rate of return in the case at bar. The Staff's motion was not made until May 25, 1960, (R. 377-8), whereas hearings on the allocation issue were concluded on December 17, 1959. Tennessee had no reason to move for omission of the intermediate decision on allocation until the Staff moved for omission of the intermediate decision on rate of return in the case at bar.

⁹ As stated above, in *Tennessee Gas Transmission Company, supra*, 18 F.P.C. at 430, 441, the Commission found that a 13.71% return on common equity was reasonable. In the instant case, the Commission reduced the return on common equity to 10.12% (R. 534).

Tennessee. The Commission's order required Tennessee to file reduced rates effective retroactively to April 5, 1960, and required Tennessee to make refunds of the differences in rates collected since April 5, 1960 (R. 524-540).

The Commission, however, failed to make any determination as to the proper method of cost allocation which should be employed in allocating the reduced over-all cost of service, resulting from its 6 1/8% rate of return allowance, among the six rate zones and various classes of service on the Tennessee system. Nor did the Commission make a determination or findings as to which of the various zone rates filed by Tennessee were unlawful, which rates should lawfully be reduced, or to whom refunds were lawfully due. Instead, the Commission left these crucial questions open for later decision, even though such later decision might result in a determination that Tennessee had reduced rates in various zones, pursuant to the interim order, which were in fact lawful in the first instance and had made refunds in the wrong amounts to the wrong customers.

Tennessee timely applied for a rehearing of the Commission's order (R. 544-576). On September 27, 1960, the Commission denied Tennessee's application for rehearing (R. 585-591).

On October 3, 1960, Tennessee filed its Petition to Review with the Fifth Circuit Court of Appeals.¹⁰ By its decision issued August 2, 1961, the Court upheld the

¹⁰ Tennessee simultaneously filed a motion for stay of the Commission's order, which was denied, Judge Wisdom dissenting. (R. 632-633).

Commission's substantive determination as to rate of return, but it held that the Commission erred in requiring a reduction in rates and refunds to be made prior to a determination of the zone allocation issue which was awaiting decision (R. 635-646).

SUMMARY OF ARGUMENT

I. Although Tennessee commenced operations in 1944, the Commission had never prescribed a method by which Tennessee's over-all costs should be allocated among the zones on its pipeline system in arriving at the rates to be charged to its customers in such zones. This important matter had been deferred on prior occasions as a result of rate settlements. Finally, it was agreed by all parties and the Commission to have this issue tried and squarely decided in the Docket No. G-11980 proceeding.

The outcome of this hotly contested issue, which was awaiting decision at the time Staff counsel made his motion for an interim rate order, could have a vital bearing not only on which particular zone rates should be reduced and to what extent, but also on whether certain of the zone rates were in fact excessive. For under some of the numerous methods of allocation proposed, there would be no rate reductions in rates in certain zones even if there were a substantial reduction in the over-all cost of service.

A. Since a decision on the zone allocation issue could have an important impact on the fixing of interim rates, the Court below correctly held that the Commission erred in setting aside Tennessee's rates before deciding the allocation issue. The Commission's action was unlawful because under Section 4(c) of the Natural Gas Act the Commission can set aside rates

only after they are found to be excessive. A determination of which of the particular zone rates were excessive and which rates should be reduced depended not only on a determination of the over-all rate of return issue, but also on the method of allocation to be applied.

The Commission abused its discretion because after it determines the allocation issue, the Commission could find that it had reduced rates by its interim order to a level below that which would be required to enable Tennessee to recover its total cost of service. Since the Commission would have no authority under the Act, in such event, to increase the rates back to the lawful level, Tennessee should have been permitted to collect its filed rates, subject to its obligation to make refunds with 7 percent interest, until the allocation issue was decided.

B. The Commission's reliance on Section 16 of the Act is misplaced. Section 16 merely gives the Commission the means to carry out the authority specifically provided by other sections of the Act. Since rates " * * * can be set aside *only* upon being found unlawful" under Section 4 of the Act, the Commission is without authority to do otherwise under the generality of Section 16 of the Act.

C. Since it was impossible for Tennessee to predict with certainty what the Commission's decision on the allocation issue would be, the Court below properly rejected the Commission's contention that it was justified in requiring Tennessee to reduce its rates at its own peril under the compulsion of the interim

^{10a} *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 342 (1953).

order which failed to prescribe the proper allocation formula to be used for such purpose.

Nor can the Commission's action be justified on the general proposition that a natural-gas company filing rates which fail to provide it with a fair rate of return cannot be heard to complain if the Commission adopts those rates. Such is not the case here because the Commission did not adopt Tennessee's filed rates. Instead, it ordered the filing of different rates which may or may not yield the prescribed fair rate of return, depending on how the Commission may later decide the cost allocation issue.

Additionally, the Commission is in error in contending that the risk is the same whether or not the Commission sets aside the rates prior to a decision on allocation. If the interim order had included a decision as to the proper allocation method to be used, the Commission obviously would have refrained from setting aside those rates which are not excessive. However, by deciding the issue separately, as here, the Commission has set aside and reduced rates in certain zones which, after deciding the allocation issue, it may find to be not excessive or not subject to as large a reduction as that required by the interim order.

D. The Commission could have avoided the problem here involved by omitting the intermediate decision on the zone allocation issue which had already been tried and briefed, as it did with the rate of return issue, and deciding the allocation issue simultaneously with the issue of rate of return.

Another lawful alternative available to the Commission for carrying out its objective, would have been to order an interim reduction in rates and provide that

any subsequent decision on allocation would apply prospectively only. In this way, the rate reduction could have been immediately passed on to the consumers, while at the same time assuring Tennessee that its rates would not be reduced below the amount called for by the Commission's decision on rate of return.

E. The cases cited by the Commission hold only that the Commission may issue interim rate orders in appropriate circumstances. But as the Commission concedes, in none of these cases was there a zone allocation issue awaiting decision at the time of the interim order. Since the Court below does not hold that the interim order procedure is unlawful *per se*, but rather that it was unlawfully applied in this case, the authorities cited by the Commission are inapposite.

F. Subsequent to the interim order issued herein, the Commission decided the allocation issue. Tennessee's estimated revenues, based on the reduced interim rates it was required to file, fall short of recovering the cost of service (at the reduced return) in certain zones by approximately \$1,500,000 based on the Commission's subsequently prescribed method of allocation. The difficulty of foretelling what allocation method the Commission would prescribe is demonstrated by the fact that the method adopted by the Commission is different than any of those proposed by the parties and the Commission's Staff.

II. Since the Commission has now issued its decision on zone allocation, affirmance of the decision of the Court of Appeals would clearly bring about a proper and just result. By setting aside the Commission's interim order, Tennessee's rates would be reinstated. The Commission could then issue a new interim order permitting Tennessee to place in effect reduced rates

as of the date its own rates became effective, but reflecting the Commission's method of allocation. In this way, the overall reduction in rates intended by the Commission would still be effectuated. Tennessee would be assured that the reductions made in each zone would be proper, and the customers in certain zones would not receive a windfall at Tennessee's expense. In other words, the effect of affirmance would be the same as if the Commission had decided the allocation and rate of return issues simultaneously, which is precisely what the Commission should have done in the first place. We fail to see how the Commission could oppose such a result, which would do justice to the consumer and the company alike.

ARGUMENT

There is no question here as to the Commission's authority generally to issue interim rate orders. Neither Tennessee nor the Court below dispute the Commission's authority to issue interim rate orders in appropriate cases. The sole problem here is whether the Commission can issue such an order where there is a zone allocation issue awaiting decision, which could have a crucial bearing not only on which zone rates should be reduced, but also on whether certain zone rates are excessive.

Tennessee would not have opposed an interim rate order prior to the disposition of other phases of the rate proceeding, if there had been no zone allocation issue pending (R. 519-521, 592). In other words, Tennessee was willing to make an interim reduction in rates and refunds, provided that the Commission would determine which zone rates should be reduced and to whom refunds were due in the event it found

upon substantial evidence that a fair rate of return was less than claimed by Tennessee.

The Commission, however, refused to make such a determination (R. 521-23, 535-37). Instead, it required Tennessee to reduce its rates and make refunds (R. 538-39), but subject to a later possible determination, after such rate reductions were made, that certain of the zone rates which Tennessee was required to reduce on an interim basis were in fact lawful in the first instance, or that some of the zone rates were reduced by too much and others by not enough and that Tennessee had made refunds in the wrong amounts to the wrong customers.

A subsequent determination of the method of allocation to be used, retroactively applied, could require Tennessee to make a further reduction in rates as to those rates which had not been reduced enough, but Tennessee would not be permitted to increase those interim rates which had been reduced too much.¹¹ This would mean, therefore, that although Tennessee had already reduced its rates to reflect the approximate \$11,000,000 called for by the Commission's decision on rate of return, the procedure established by the Commission could require Tennessee to make an over-all reduction in rates in excess of the \$11,000,000 applicable to that issue, even though its decision as to rate of return would justify no more than an \$11,000,000 over-all reduction in

¹¹ The Commission interprets the Act as precluding it from increasing rates above those on file with the Commission. *Atlantic Seaboard Corp.*, 11 F.P.C. 43, 63-65 (1952). Since Tennessee's rates were set aside by the interim order, the Commission deems those rates as no longer being on file, even though certain of those rates may be justified based on the later decision on allocation.

rates. In these circumstances, Tennessee would be denied the opportunity to earn the 6½ percent rate of return to which the Commission said it was entitled. For these reasons, Tennessee objected to the interim order procedure as applied in this case, and, for the same reasons, the Court below found the procedure as applied herein to be unlawful and unfair.

I

THE INTERIM ORDER PROCEDURE AS APPLIED IN THIS CASE IS UNLAWFUL AND UNFAIR.

While the Commission concedes that the interim order procedure as applied in this case could result in Tennessee being denied rates which would permit it to earn a "reasonable rate of return," the Commission contends that such procedure is, nevertheless, lawful. Moreover, the Commission argues, there was only a remote possibility of injury to Tennessee (Br. p. 40).

Before dealing with the various arguments made by the Commission and the virtually identical arguments made by the City of Pittsburgh and the Commonwealth of Pennsylvania,¹² we believe it would be helpful to discuss at this juncture in greater detail the background of the zone allocation issue and the relationship of that issue to the matters here involved.¹³

¹² Since the arguments made by the City of Pittsburgh and the Commonwealth of Pennsylvania are almost identical to those made by the Commission, most references herein will be to the Commission's brief.

¹³ Subsequent to the interim order here involved, the Examiner issued his decision on zone allocation which contains an extensive history of that issue, from which the following discussion, as to background is taken. *Tennessee Gas Transmission Company*, Docket No. G-11980, Examiner's Decision issued February 13, 1961 (*mimeo.*, pp. 1-10, unreported). A copy of this decision has been

The Background of the Zone Allocation Issue

Tennessee does not have a system wide rate which applies to all services of a similar character regardless of the location of the sale and delivery of gas. Because of the length of the Tennessee pipeline system, six rate zones and rate differentials among those zones were heretofore established as a result of rate settlements entered into the early 1950's between Tennessee, its customers and the Commission's Staff, with the approval of the Commission.

In these settlements, there were conflicting views among the parties as to the method of allocation that should be used in the future to arrive at the zone rate differentials. In order to reach a settlement, the parties simply agreed to certain zone rates, without agreeing to the method of allocation to be applied in the future, with the understanding that this issue would be litigated in some future rate proceeding. From the time Tennessee first initiated service in 1941 until 1954, its rates had always been arrived at as a result of such rate settlements as approved by the Commission.

During the course of hearings with regard to a rate filing made in November, 1954, the New England zone customers raised the issue of zone allocation. The

adjudge with the Clerk of this Court. On February 13, 1962, the Commission issued its Opinion No. 352 on zone allocation, which, for the most part, adopts the Examiner's decision. *Tennessee Gas Transmission Company*, 42 PUR 3d 145, pending on review *sub nom. Manufacturers Light and Heat Co. v. Federal Power Commission*, CADC No. 17064. The Commission's opinion also sets forth some of the background with regard to the zone allocation issue (42 PUR 3d at pp. 149-50).

Commission directed that such issue be deferred until after the cost of service issues were heard in that case. At the conclusion of the hearings on cost of service, Tennessee moved that the Commission decide those issues and issue an interim rate order based thereon. Tennessee further proposed that any subsequent decision as to zone allocation be applied prospectively only. The Commission granted Tennessee's motion insofar as it requested that a decision be made on the cost of service issues, but it held that it would be "unfair and improper" to issue an interim rate order while the issue of zone allocation was still pending. The reasons given by the Commission for not issuing an interim rate order in that case are the very reasons which the Commission now contends are unimportant.¹ Thus, the Commission there stated:

The pleadings pose the questions of whether it is appropriate and in the public interest for the Commission *at this time and on the present record* to consider and determine separately the issues relating to total cost of service and rate level and to reserve for subsequent decision the issue raised concerning zone rate differentials; and should the intermediate decision procedure be omitted:

* * * * *

Fulfillment of the request of Tennessee that determination be now made as to its total cost of service and the rate level would not only require determination as to the proper method of allocating the "total" between jurisdictional and non-jurisdictional sales, but it would require also present determination as to the proper method

¹ *Tennessee Gas Transmission Company*, Docket No. G-5259, order issued September 29, 1956 (unreported). A copy of this order appears in Appendix B to the Commission's brief (pp. 52-61).

of allocating the jurisdictional portion of the total between the several zones of service, or at least, a determination that the present zone boundaries and rate differentials should be maintained for sales made on and since December 15, 1954, and continuing until final order in this proceeding. It is not possible at this incomplete state of the proceeding to determine proper zone boundaries and what method of allocating costs between zones would be fair and equitable.

* * * * *

Our experience tells us that, if in the future a change in Tennessee's zone boundaries or rate differentials is in order, the effect of the resultant rate on particular customers will differ dependent upon what cost of service is found proper here. *On this record, however, it is not possible to now determine what the effect upon particular customers will be until resolution of the cost of service and zone issues.*

Thus, we are of the opinion that it would be not only premature for us to grant that part of Tennessee's motion requesting that we at this time fix rates to be effective on and after December 15, 1954, it would also be *unfair and improper.*

In January, 1957, Tennessee filed new rates with the Commission in Docket No. G-11980 to recover increases in costs which occurred after its previous rates were filed in 1954. At the time such new rates were filed no decision had, as yet, been rendered by the Commission on the cost of service issues in the previous rate case and no further hearing had been held on the zone allocation issue. Thus, in order to expedite the conclusion of the prior proceeding, Tennessee moved that the Commission dismiss the zone allocation issue in that proceeding and have that issue

squarredly decided and finally resolved in Docket No. G-11980. All parties agreed to this procedure and the Commission granted the motion by order issued September 5, 1957.

After hearings in the Docket No. G-11980 proceeding commenced, the Commission by order issued April 30, 1959, directed that the determination of the allocation issue be expedited, stating that a determination of this issue would aid in the disposition of subsequent cases. To this end, it severed the zone allocation issue for separate and prior hearing and determination in the Docket No. G-11980 proceeding.

Hearings with regard to the zone allocation issue proceeded and were completed in December, 1959. Final briefs on that issue were submitted in April, 1959. Thus, at the time Staff counsel made his motion for an interim order in the case at bar the allocation issue in Docket No. G-11980 was awaiting decision.

It was apparent at the time Staff counsel made his motion that the outcome of the zone allocation issue could have a material effect on any rates fixed in the case at bar, whether such rates were fixed on an interim or final basis. First, as indicated earlier, the Examiner had already ruled that the determination of the allocation issue in Docket No. G-11980 would be controlling in the case at bar (R. 50-51).¹⁵ Secondly, diverse methods of allocation had been proposed which yielded substantially different results in allocating the same total cost of service among the six rate zones.

¹⁵ The Commission has since held that the decision on zone allocation in Docket G-11980 would apply to all future cases. "Inquies and until it may be demonstrated at some later date that a change is required." *Tennessee Gas Transmission Company, supra*, 42 PUR 3d at p. 150.

(R. 594). The evidence showed that even if there were a substantial reduction in the overall cost of service submitted by Tennessee, there would be no reduction in rates in certain zones depending on the method of allocation selected (R. 597-98).¹⁶ It is, therefore, evident that without also deciding the issue of zone allocation the Commission could not determine, simply on the basis of its decision as to rate of return, which particular rates in the various zones were excessive and the extent to which they were excessive.

Petitioners contend, nevertheless, that the interim order procedure as applied in this case is lawful. In essence, Petitioners argue that Tennessee was not entitled to know which particular rates to reduce and by how much. They assert that Tennessee was required to make rate reductions and refunds at its own peril. For the reasons shown below, Petitioners' arguments are without merit.

A. The Commission Cannot Set Aside Rates Until They Are Found Excessive

The order under review is fatally defective because, without first deciding the zone allocation issue, the Commission could not validly make the statutory finding that the various filed rates, which it ordered reduced, were unjust or unreasonable; nor could it validly determine the rates to be thereafter charged, as required by the Act.

The rates here involved were filed pursuant to Section 4 of the Natural Gas Act. As this Court

¹⁶ For example, although the Staff proposed a substantially lower cost of service than Tennessee in the Docket G 11989 proceeding, one of the proposed methods of allocation as applied to the Staff's cost of service would result in more than \$5,000,000 more costs being allocated to one zone than Tennessee's filed rates could recover (R. 597-598).

explained in *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 342-3 (1956), under Section 4(d) of the Act a natural-gas company is required to give 30 days' notice as to the effective date of the new rates. Under Section 4(e) the Commission has authority within the 30-day period to suspend the effective date of the new rates for five months. In this event, upon motion of the company, the rates then become effective.

Section 4(e) of the Act further provides the Commission with authority * * * to enter upon a hearing concerning the lawfulness of such rate * * * and after full hearings, * * * the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it [the rate] had become effective. * * *. This has been construed¹⁷ as giving the Commission the same authority it has under Section 5(a) of the Act, which provides that, "Whenever the Commission, after a hearing * * * shall find that any rate * * * is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate * * * to be thereafter observed and in force, and shall fix the same by order. * * *"

Unlike Section 5(a), where orders of the Commission have prospective effect only, the Commission may, under Section 4(e) of the Act, make its order retroactive to the date the rates became effective. Thus, the Commission may require the company to collect its new rates subject to a refund obligation and * * * upon completion of the hearing and decision * * * the Commission may require the com-

¹⁷*United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, *supra*; *Hoppe Natural Gas Co. v. F.P.C.*, 196 F. 2d 803, 805 (4th Cir. 1953).

pany * * * to refund, with interest, the *portion of such increased rates or charges* by its decision found not justified. * * *

"As this Court pointed out in the *Mobile* decision, *supra*, the basic authority given the Commission under Sections 4(c) and 5(a) is to set aside and modify rates, but such rates * * * can be set aside *only* upon being found unlawful by the Commission" (350 U.S. at 341-43).¹⁸ Notwithstanding this restriction on the Commission's authority to set aside rates, the Commission argues as follows (Br., p. 20):

"In holding that, in the absence of a Commission decision on cost allocations, there was 'no basis for determining which of the filed rates in specific zones were unlawful' (R. 642), the court below misconceived the test of validity applicable to an interim order. For the test is not whether there can be a resolution of all questions which relate to the lawfulness of the rate but whether the sufficiency of the attempted justification of a component part of the increased rate can be decided separately * * *

The defect in the Commission's argument is that while the rate of return is a separate component of the cost of service and can be decided separately, its decision on rate of return, as a separate issue, only determines the total amount of the reduction in the over-all cost of service. What this means in terms of reduced rates for the respective zones, however, depends on the method selected by the Commission for allocating such over-all cost of service among the zones.

¹⁸ To the same effect see *Colorado Interstate Gas Co. v. F.P.C.*, 142 F. 2d 943, 954 (10th Cir. 1944), affirmed, 324 U.S. 581 (1945).

As stated earlier, Tennessee would not have opposed the interim order procedure in this case if the Commission would have determined which particular rates should be reduced and what refunds should be made to the customers in the various zones, in the event it found upon substantial evidence that a fair rate of return was less than claimed by Tennessee. What Tennessee objected to was the Commission's procedure which subjected Tennessee to the hazard of being later required to make further retroactive rate reductions (after decision of the zone allocation issue) in excess of the amount necessary to reflect the reduction in rate of return and, thereby, depriving Tennessee of the rate of return which the Commission found proper.

B. Section 16 of the Act Does Not Empower the Commission To Do Acts Which Are Beyond Its Authority Under Other Sections of the Act

As support for its authority to issue the interim order here involved, the Commission relies heavily on Section 16 of the Natural Gas Act which provides it with authority to issue rules, regulations and orders "as it may find necessary or appropriate to carry out the provisions of" the Act (Br., pp. 17, 50). The Commission argues that a primary aim of the Act is consumer rate protection, and, hence, it has authority under Section 16 of the Act to carry out that aim (Br., p. 17). But, as the Commission has observed on a prior occasion, "this Section does not * * * grant the Commission any power to issue an order which does not have its genesis elsewhere in the act." *Willmut Gas and Oil Co. v. United Gas Pipe Line Co.*, 12 F.P.C. 132, 142 (1953); Cf. *F.P.C. v. Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, 508 (1949).

For example, the Commission under the rate provisions of the Act, Sections 4 and 5, could not order a rate reduction without notice and hearing. While noncompliance with notice and hearing requirements may expedite rate reductions, this does not mean that the Commission has authority to issue such an order under Section 16 of the Act. Section 16 merely gives the Commission the means to carry out the authority provided by other sections of the Act. Thus, whether or not the Commission had the authority to issue the interim rate order here involved does not depend on the interpretation of Section 16 of the Act, but rather on the rate provisions of the Act, namely Sections 4 and 5. For, the question in this case is not whether the Commission has authority to issue interim orders in appropriate cases, but whether its order meets the standards imposed by Sections 4 and 5 of the Act. Thus, if rates " * * * can be set aside *only* upon being found unlawful" under Sections 4 and 5 of the Act, the Commission is without authority to do otherwise under Section 16 of the Act.

C. The Commission's Attempted Justification for the Interim Order Procedure as Applied Herein Is Without Merit

The Commission asserts that since Tennessee has the burden of proof under Section 4(c) of the Act, it was justified in ignoring the evidence before it on the zone allocation issue and in reducing Tennessee's rates prior to the disposition of that issue. While the Commission recognizes that this may result in Tennessee being unable to earn a fair return, it argues that the Commission has no obligation under the act to guarantee Tennessee a fair return. Moreover, the Commission argues, Tennessee itself may file rates which yield an inadequate return and the interim order procedure as applied herein does not increase that risk. Thus, the Commission claims, it was justified

in requiring Tennessee to reduce its rates at its own peril pending the decision on the zone allocation issues (Br., pp. 26-28).

While it is true that the Commission does not guarantee Tennessee that it will earn a fair rate of return, since this depends, in part, on the amount of business that Tennessee will do in the future, it is well established that a regulated company is entitled to an opportunity to earn a fair return. *Bluefield Waterworks and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679, 692 (1923). The procedure employed by the Commission herein, however, could deprive Tennessee of such an opportunity by setting aside certain of the zone rates which the Commission may later find (1) should not have been reduced at all, or (2) should have been reduced to a lesser extent than required by the interim order.

Nor can the Commission's action be justified by the possibility that, even in the absence of an interim order, Tennessee's filed rates may be too low in some zones to yield a fair rate of return. The Commission argues that since Tennessee has such a risk at the outset, the interim order does not increase that risk (Br., p. 26).

It is true that a natural-gas company may file rates which in the aggregate are too low to yield a fair rate of return. In those circumstances, the injury to that company would be the result of its own act. Such is not the case here. In the case at bar it is the Commission's action, rather than any act on the part of Tennessee, which would deprive it of rates yielding a fair rate of return. Cf. *F.P.C. v. Sierra Pacific Power Co.*, 350 U.S. 348, 355 (1956).

Moreover, the Commission is in error in contending (p. 26) that the risk is the same whether or not the Commission decided the allocation issue simultaneously with the issue of rate of return. When the Commission decides the issues simultaneously, either on an interim order basis or at the conclusion of the proceedings, and finds that some of the rates are below that necessary for a fair return, obviously it would not set aside those rates as being excessive. Also, Tennessee could then correct the rate upward to a lawful level. But by deciding these issues separately as here, the Commission could set aside and reduce rates which not only are not excessive, but which are below a lawful level. Tennessee, in such circumstances, is also denied the opportunity of correcting the rate to a lawful level until the allocation issue is decided. Thus, the interim order procedure as applied herein clearly exposes Tennessee to much greater risk than if these issues were decided simultaneously.

Requiring Tennessee to reduce its rates at its peril by guessing what the outcome of the allocation issue will be is particularly unfair in light of the history of that issue. As explained earlier, the Commission had never previously determined a method of zone allocation for the Tennessee system. Nor had it in any other case prescribed a zone allocation formula to be applied in all cases. Thus, the issue was wide open and what the outcome of that issue would be was anybody's guess. As this Court has aptly observed, allocation of costs " * * * is not a matter for the slide rule" but instead "involves judgment on a myriad of facts". *Colorado Interstate Gas Co. v. F.P.C.*, 324 U.S. 581, 589 (1945).

The importance of a decision on this issue in pending and future rate cases is clearly shown by the Commission's Opinion on zone allocation subsequently

issued in Docket No. G-11980, wherein the Commission stated (*Tennessee Gas Transmission Co., supra*, 42 PUR 3d at 149):

"The selection of appropriate methods of cost allocation and the explication of the underlying principles by which such methods can be evaluated are among the most important responsibilities of this commission. Although eighteen years have elapsed since Tennessee was granted its original certificate, this is the first case in which the allocation issues arising out of the complex operation of the Tennessee system have been fully heard and presented to the commission on a complete record. *Since the allocation method is a fundamental part of every pending and future Tennessee rate case, it is imperative that these basic issues be determined herein.* * * *

A zone allocation issue is principally a contest among customers, since the problem involved is not the total cost of service, but how that total cost should be divided among customer zones. The pipeline is obviously most concerned with recovering its total cost of service regardless of how such total is divided. As could be expected, the customers in each rate zone sponsored or favored a method of allocation, which allocated the least part of the total cost to that zone. For this reason, diverse and complex methods of allocation were submitted, which yielded substantially different results for a particular zone.

The Commission's contention that, because Tennessee has the burden of proof, it may set aside the rates and ignore the contested allocation issue, which may have a crucial bearing on the rates being set aside, is clearly without merit. As the Commission itself held in its Opinion on the allocation issue, once the evidence on allocation has been presented, it is

bound to arrive at a method of allocation on the basis of the entire record *regardless of who presented the evidence and who has the burden of proof*. *Tennessee Gas Transmission Company, supra*, 42 P.U.R. 3d at 149.¹⁹

The unfairness of the Commission's procedure is particularly acute where an issue as to zone allocation has been raised and sharply contested; and where, as here, no prior decision as to zone allocation has been rendered. The difficulty of foretelling what the outcome of such an issue will be is demonstrated by the fact that the Commission ultimately selected a method of allocation which was different from any of those presented by the parties. In these circumstances, the contention by the Commission that it was justified in requiring Tennessee to reduce its rates at its own peril prior to deciding the allocation issue is clearly without merit. Such a procedure relegates rate-making into a poker game in which only the pipeline can be the loser. The Commission's function is to arrive at lawful rates—not to employ procedures which may saddle a company with rates which cannot recover the cost of service.

In arguing that Tennessee has the burden of proof, the Commission overlooks its own obligations under the Act. As stated earlier, the Commission is required to hold a "full hearing" with regard to the rates and can set aside the rates "only upon being found unlawful." In setting aside rates, it is the Commission's obligation, not Tennessee's, to determine which rates are excessive, the extent to which they are excessive and what refund should be made. Since the Com-

¹⁹ Cf. *American Louisiana Pipe Line Company*, F.P.C. Opinion No. 363 (1962; unreported).

mission cannot make such a decision prior to the determination of the allocation issue, it cannot lawfully require Tennessee to reduce its rates at its own peril subject to a retroactive determination that Tennessee had reduced the wrong rates and made refunds to the wrong customers.

The contention of the Commission (Br., pp. 30-31), that the decision below would preclude the Commission from ever issuing interim rate orders and would require the Commission to decide all phases of the rate proceeding prior to issuing a rate order, is plainly incorrect. Where there is conflicting evidence before the Commission as to the lawfulness of the rates, the Court below merely requires that the Commission decide those matters necessary to determine whether the rates are lawful. In the case at bar, this required only a decision on the allocation issue pending before the Commission as well as the issue of rate of return, and would not, as the Commission claims, require the Commission to decide all phases of the rate proceeding prior to issuing an order as to rates.

Indeed, the Commission has experienced no difficulty in applying the interim order procedure since the issuance of the decision below. Recently, the Commission granted a motion by its Staff to invoke the interim order procedure in a rate proceeding involving El Paso Natural Gas Company, wherein the Commission's Staff urged:

... * * the *Tennessee* decision (*Tennessee Gas Transmission Company v. F.P.C.*, 293 F. 2d 761) is distinguishable from these proceedings in that

²⁰ *El Paso Natural Gas Company*, Docket No. G-4769, *et al.*, order issued December 27, 1961. A copy of this order is attached as Appendix A to Tennessee's Brief in Opposition to the Petitions for Certiorari.

here there are no other issues ripe for decision whereas in *Tennessee* the basis of the court's refusal to allow the interim order to become effective was the fact that *the allocation issue was ripe for decision*; * * *

D. The Commission Had Lawful Alternatives Available for Carrying Out Its Objective

The Commission could have avoided the problem here involved by omitting the intermediate decision on the zone allocation issue which had already been tried and briefed, as it did with the rate of return issue, and deciding the zone allocation issue simultaneously with the issue of rate of return. In this way an interim rate order could have been lawfully issued prior to the disposition of other phases of the proceeding, and if the rate of return was reduced, Tennessee would have known which particular rates should be reduced and to what extent.

While a decision on zone allocation would have entailed a short delay in the issuance of an interim rate order,²¹ the consequences of such a delay would

²¹ The Commission (Br. pp. 37-8) asserts that it was unable to reach a decision on allocation until February 6, 1962, approximately 18 months after the interim order, and that it required two oral arguments before it could reach its decision. What the Commission fails to point out, however, is that this inordinate delay was caused by its own failure to omit the intermediate decision. Tennessee advised the Commission when it requested omission of the intermediate decision that the Examiner had informed all parties that he would be unable to begin working on his allocation decision for some months because of his involvement in other cases (R. 519-52). After the Examiner issued his decision, there was further delay caused by the appointment of new commissioners resulting from the change in administrations. Thus, after one oral argument, there was a reargument before the new commissioners in September, 1961. It took the new Commission in the ordinary course, only 5 months to decide the issue from the time of oral argument.

have been negligible. The reduction in rate of return when translated into reduced rates for the average household consumer amounts to approximately 15¢ per month in a gas bill. Thus, awaiting the outcome of the allocation issue would have required that the average householder pay approximately 15¢ per month, subject to refund with 7% interest, until the allocation issue was decided.²² On the other hand, by requiring Tennessee to reduce its rates prior to a decision on the zone allocation issue, the Commission exposed Tennessee to the possibility that it would be unable to recover millions of dollars of its out-of-pocket costs in rendering service to certain zones.

The Commission argues, however, that it was justified in not omitting the intermediate decision on the allocation issue because of the complexity of that issue. Even assuming *arguendo* that this is correct, this does not mean that the Commission can issue an interim rate order prior to the resolution of the inter-related allocation issue. The Court below does not hold that the Commission erred in failing to omit the intermediate decision on allocation, but rather it holds that the Commission did err in setting aside Tennessee's rates prior to the time that they could be determined to be unlawful.

The Commission also asserts (Br., pp. 32-33) that although Tennessee is obligated to make refunds with 7% interest, the refund provision in the Act is an

²² Tennessee's total annual deliveries of natural gas in the test year ending July 31, 1959 were approximately 700,000,000 Mcf. Thus, the \$11,000,000 over-all reduction amounts to approximately 1.7¢ per Mcf on a straight volumetric basis. The average residential consumer uses approximately 104 Mcf of gas annually or approximately 9 Mcf on a monthly average basis. *American Gas Association, Gas Facts for 1960*, page 96.

imperfect mechanism and an inadequate substitute for the interim order procedure. In this regard, the Commission erroneously contends that the refund provision was not intended for consumer protection, but was intended to permit the natural gas company to collect its rates subject to refund pending a determination as to lawfulness (Br., p. 35).²³

Apart from other fallacies in the above argument, the short answer is that if the Act entitled Tennessee to collect its rates pending a determination as to lawfulness, the Commission cannot ignore this requirement, regardless of its views as to possible inadequacies of the refund provisions of the Act. Whether or not the interim order procedure is a desirable tool for expediting rate cases is beside the point. The Court below does not hold that the interim order procedure is unlawful *per se*, but rather that it was unlawfully applied in this case.

Moreover, there were still other lawful alternatives available to the Commission which would have permitted it to carry out its objective. The Commission could have ordered an interim reduction in rates, but held that any new method of allocation subsequently adopted would apply prospectively only, in arriving at zone rates. In this way the rate reductions, if any, could immediately be passed on to the consumers. At the same time, Tennessee would be assured that to the

²³ The contention that the refund provision in Section 4(c) of the Act was not intended for consumer protection is clearly incorrect. Congress was aware that an unreasonable suspension period would be unconstitutional. *Hopie Natural Gas Co. v. F.P.C.*, 196 F. 2d 803, 809 (4th Cir. 1952). Thus, in order to protect the consumer while the case was pending after the suspension period, it enacted the refund provision. Cf. *Atlantic Refining Co. v. Public Service Commission of New York*, 360 U.S. 378, 390 (1959).

extent that it had made the over-all reduction in rates ordered by the Commission, that reduction would be final as to the issue decided.²⁴

The operation of the above type of interim order would have been the same as that approved by the Seventh Circuit and later by this Court in the *Natural Gas Pipeline* case²⁵ cited by the Commission (Br., p. 22). There the Commission in a Section 5(a) investigation heard evidence as to rate of return and issued an interim order requiring the pipeline to reduce its rates without prescribing the method of allocation. However, since the Commission orders under Section 5(a) have prospective effect only, a subsequent order as to allocation would have had no retroactive effect on the interim reduction. In approving this procedure, the Court of Appeals noted that while the action of the Commission was "irregular" and "unusual," it was in no way "harmful" to the pipeline (120 F. 2d at p. 631).

E. The Commission Has No Judicial Sanction For Applying the Interim Order Procedure in a Case Such as This

In addition to the *Natural Gas Pipeline* case, *supra*, which is obviously distinguishable from the type of interim order issued herein, for the reasons discussed above, the Commission cites (Br., pp. 22-25) as authority the decisions in *Panhandle Eastern Pipe Line Co. v. F.P.C.*, 236 F. 2d 606 (3rd Cir. 1956), and *State Corporation Commission of Kansas v.*

²⁴ As Tennessee indicated to the Commission, it would have no objection to this type of interim rate order (R. 599).

²⁵ *Natural Gas Pipeline Co. v. F.P.C.*, 120 F. 2d 625, 631 (7th Cir. 1941); reversed on other grounds, *F.P.C. v. Natural Gas Pipeline Co.*, 315 U.S. 575, 584 (1942).

F.P.C., 206 F. 2d 690 (8th Cir. 1953), which involved interim rate orders issued under Section 4(c) of the Act.²⁶

The Commission concedes, however, that the issue here involved was not raised or decided in the above cases (Br. 29-30). Indeed, in neither of the above cases was there an interrelated allocation issue awaiting decision at the time of the interim order. The Commission contends only that the interim orders in these cases did not preclude the possibility of such an issue being raised at a later stage of the proceeding (Br. p. 30). Since the above hypothetical possibility was not raised on review and therefore not considered, these cases can hardly be regarded as authority for the issue here involved. Moreover, the possibility that an allocation issue might have been raised in the future is a far cry from the facts here involved where the issue was not only actually raised, but heard, briefed and awaiting decision at the time of the Commission's interim order.

The backgrounds of the *State Corporation Commission* case (involving Northern Natural Gas Company) and the *Panhandle* case are similar. In each of the above cases, the Commission issued interim orders dismissing rate filings by those companies insofar as the filings raised issues which had just been decided in prior proceedings involving the same companies. In the case of *Panhandle*, the Commission, just 75 days prior to the interim order, had decided rate design

²⁶ The Commission also cites a number of other cases (Br. p. 22) purporting to show that courts have approved measures similar to the interim order. But none of these cases establish that the Commission may set aside rates prior to the time that they can be found unlawful. These cases, therefore, are inapposite.

and zone allocation issues for the Panhandle system. The interim order made it clear that the Commission would not retry these issues and that the interim reduction in rates should be based on the same allocation methods just decided (See 236 F. 2d at p. 611). Thus, as the Court pointed out, the issues decided on an interim basis were "severable" (236 F. 2d at 608).

Northern, on the other hand, had single system-wide rates and, therefore, no allocation to zones was necessary. Insofar as allocation of costs between jurisdictional and nonjurisdictional customers was concerned, the Commission dismissed that issue since a method of allocation had just been prescribed in the previous case. Thus, in ordering the interim reduction, the Commission set forth the allocation factors to be used. *Northern Natural Gas Company*, 11 F.P.C. 278 and 11 F.P.C. 1324, 1327-29 (1952).

F. The Commission's Contentions With Regard to the Remoteness of Injury to Tennessee Are Without Merit

While the Commission considers the probability or improbability of injury to Tennessee stemming from the interim order procedure as applied herein to be immaterial to the issue involved, it claims that there was no justification for assuming that Tennessee would be injured, because such a possibility was

²⁷ The City of Pittsburgh (Br. p. 22) contends that in the above two cases there remained allocation issues to be disposed of. In the *Panhandle* case the only allocation issue remaining was a special allocation problem dealing with Panhandle's hydrocarbon extraction operations. Any change in this allocation subsequently would only result in a further reduction in rates and not an increase in the rates as would be the case here. As to the *Northern* case, we know of no allocation issue that was pending. The Commission in its brief only claims that such an issue might have been raised after the interim order.

remote (Br., pp. 39-41). As support for this contention, the Commission notes that at the time of the Commission's interim order there remained substantial cost of service questions to be considered in the second phase of the proceeding. Additionally, the Commission refers to the fact that recently the Examiner issued his decision on the second phase of the proceeding recommending a further reduction of \$25,000,000 in the cost of service. The Commission claims that if his decision is upheld, the interim rates are adequate to recover the cost allocated to zones based on the method of allocation subsequently prescribed by the Commission (Br., p. 41).

In the first place, the Examiner's recommendation is not final and Tennessee has filed extensive exceptions to his recommendation which are now pending before the Commission. If certain of these exceptions are granted, Tennessee will not be able to recover its cost of service in certain zones if the Commission's method of allocation is retroactively applied.

Secondly, the Commission's order must be reviewed as of the time it was issued and, therefore, the Examiner's subsequently issued decision has no bearing on the issue. As shown by the record, there was a substantial possibility at the time of the interim order that Tennessee would be unable to recover its cost of service based on proposed methods of allocation then pending before the Commission (R. 597-599).

Indeed, Tennessee's estimated revenues based on the interim rates it was required to file, fall short of recovering the cost of service (at the reduced return) in the New England zone by approximately \$1,500,000 based on the Commission's subsequently prescribed method of allocation (Appendix A, hereto).

II

**AFFIRMANCE OF THE DECISION BELOW WOULD BRING ABOUT
PROPER AND JUST RESULT**

As stated earlier, on February 6, 1962, the Commission issued its decision in Docket No. G-11980 determining the method of zone allocation to be used for the Tennessee system. *Tennessee Gas Transmission Company, supra*. It is clear from the Commission's Opinion (42 PUR 3d at 150) and from the Examiner's ruling previously mentioned (R. 50-51), that the method of allocation adopted by the Commission will apply to the case at bar.

Since the Commission has now issued its decision on zone allocation, affirmance of the decision of the Court below would clearly bring about a proper and just result. By setting aside the Commission's interim order, Tennessee's filed rates would be reinstated. The Commission could then issue a new interim order permitting Tennessee to place in effect reduced rates as of the date its own filed rates became effective, but reflecting the method of allocation which the Commission has now decided to be proper.²⁸ In this way, the over-all reduction in rates called for by the Commission's reduction of the rate of return claimed by Tennessee would be effectuated. Tennessee would then be assured that the reductions made would be proper. This would simply prevent customers in certain zones from receiving a windfall at Tennessee's expense. In other words, the effect of affirmance would be the same as if the Commission had decided

²⁸ Since the Commission's allocation decision is pending on review in *Manufacturers Light and Heat Co. v. F.P.C.*, CA-DC No. 17064, we would not oppose the mandate of the court below being held in abeyance until the review proceeding in the above case is completed.

the allocation and rate of return issues simultaneously, which is what it should have done in the first place. We fail to see how the Commission could oppose such a reasonable and lawful result.

CONCLUSION

For the reasons set forth herein, we respectfully urge that the judgment of the Court of Appeals should be affirmed.

Respectfully submitted,

HARRY S. LETTMAN

Attorney for Tennessee

Gas Transmission Company

W. C. BRADEN, JR.

402 Solar Building

Washington 5, D. C.

HARRY S. LETTMAN

JACK WERNER

HAROLD L. TALISMAN

317 Wyatt Building

Washington 5, D. C.

Attorneys for Tennessee

Gas Transmission Company

September 22, 1962

APPENDIX A

The following shows: (1) The estimated revenues based on the interim rates Tennessee was required to file with (2) the cost of service (at the reduced return) submitted pursuant to the Commission's interim order²⁹ allocated to zones by the Commission's subsequently prescribed method of allocation. Column (3) shows those zones in which there is a deficiency in recovering the allocated cost.

Zones	(1) Revenues at Interim Rates	(2) Allocated Cost	(3) Deficiency
Southern	\$32,335,232	\$32,339,538	\$ 4,306
Central	21,698,723	21,769,055	70,332
Eastern	78,927,166	78,737,926	
Northern	57,110,143	56,681,448	
New York	43,341,853	42,721,460	
New England	32,937,267	34,366,150	1,428,883
Total Deficiency			\$1,503,521

²⁹ Excludes costs related to jurisdictional transportation services and non-jurisdictional sales and transportation. The revenues shown for the New York zone, column (1), include approximately \$156,000 for sales to Trans-Canada, which the Commission did not include in Appendix C to its brief.